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A Conceptual Framework to Guide Research on Private Sector Development in Developing Countries

Simon White

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Abstract

In the last decade, international development and donor agencies have paid increasing attention to the role of the private sector as an engine for economic growth and poverty reduction in developing and transition economies. Within this context, greater attention has also been given to the role of markets in development. In this paper, Simon White explores the role of private sector development (PSD) in development research and initiatives. The paper presents findings, conclusions and recommendations on PSD to guide the PSD-related investments of IDRC's Globalization, Growth and Poverty (GGP) programme initiative, and to help IDRC to reach a common vision of PSD, across all programming units, for future PSD-related investments. The paper first examines the concepts related to PSD and identifies the key rationale for PSD support by bilateral and multilateral donor agencies. Then, it explores the ways in which donor agencies support PSD and presents an account of the trends that influence the design and delivery of PSD support interventions. The major debates and controversies that surround the support of PSD are then examined and a number of suggestions are made to IDRC for a PSD research agenda.

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I. Introduction

In the last decade, international development and donor agencies have paid increasing attention to the role of the private sector as an engine for economic growth and poverty reduction in developing and transition economies.[1] Within this context, greater attention has also been given to the role of markets for development. Since private sector development (PSD) revolves around access to markets and the capacity of domestic entrepreneurs to identify and pursue new market opportunities, this area of work has been found to be extremely relevant to pro-poor development approaches.[2] Similarly, in an age of globalisation and a more closely integrated world economy, the international flows of private investment are considered as a potent resource for economic growth.

The focus on markets and investment has been accompanied by a better understanding of the factors that contribute to the creation of a more diverse, competitive and robust private sector. While attention has long been given to addressing the internal constraints of enterprise growth (e.g. through the provision of financial and business development services), greater attention is now given to the broader conditions and systems in which private enterprises operate. As support for PSD continues and the areas of focus shift to a more market-driven and systemic approach, new questions emerge regarding the policies and practices that ensure PSD support leads to economic growth and poverty reduction. A systemic approach to the support of PSD presents new opportunities for PSD to contribute more effectively to key social and economic development goals. However, it also raises a range of questions that have hitherto not been fully answered and which form the basis of further research.

1. For examples of donor private sector development strategies see AusAID (2000), ADB (2000), Cida (2003), DFID (2004), OECD (1995, 2004), Sida (2001), UNDP (Commission on the Private Sector and Development 2004) and World Bank (2002b).

2. For further information on the role of markets in pro-poor development see DFID (2000), OECD (2004a), Sida (2003) and World Bank (2002a).

This report has been prepared for the Private Sector Development Taskforce (PSDTF) of the International Development Research Centre (IDRC). The PSDTF was formed in 2004 to explore PSD as a research theme and to identify possible programme niches for the Centre. It presents findings, conclusions and recommendations on PSD that will guide the PSD-related investments by the Globalization, Growth and Poverty (GGP) programme initiative and help the IDRC reach a common vision of PSD for future PSD-related investments across all programming units.

The GGP programme initiative provides financial support for a large number of projects. Its goal is "to support policy reforms in developing countries aimed at promoting inclusive growth and poverty reduction and appropriate international integration strategies, by generating necessary evidence and knowledge and strengthening capacities for their production and use in inclusive policymaking" (IDRC 2006, 15). In achieving this goal, the GGP programme initiative has four objectives:

1. Provide solid, locally grounded evidence on the patterns and drivers of inclusive economic growth and poverty reduction to enable governments and non-government actors in developing countries to design suitable policies and programmes.
2. Inform policymakers and civil society actors of the opportunities and challenges in reducing inequality and poverty through appropriate trade strategies and by situating markets (domestically and internationally) within proper contexts of rules and regulations.
3. Develop policy analyses, proposals, and recommendations that enable governments and non-government actors in developing countries to design equitable and effective social protection systems.
4. Enrich policy analyses conducted by researchers in developing countries with enhanced understanding of the dynamics and non-income dimensions of poverty and inequality, the political economic implications of pro-equity reforms, and the appropriate levels (local, national, international) of pro-equity policy interventions.

The GGP programme initiative has three research themes, two of which have particular relevance to the support of PSD.[3] The first deals with the patterns and drivers of inclusive growth. This involves research into the sectors, regions, and types of firms whose growth is most likely to reduce inequality and poverty. It examines policy changes that promote enterprise development, stimulate investment, and enhance productivity in these areas.

The second deals with the shape, functioning, and phasing of appropriate combinations of market and non-market institutions to promote inclusive growth. This involves research into the poverty and equity implications of trade liberalisation and how those considerations can be made more central in policymaking. It also involves research into the implications of a concentration of market power, uncompetitive practices and failures of regulation, and the design and phasing of competition and regulation regimes for promoting inclusive growth. Attention is also given to the nature of non-economic institutions associated with failed or missing markets and the extent to which they may become pro-equity alternatives rather than producing cycles of exclusion, poverty, and deprivation.

With the above themes in mind, this report defines the component features of PSD support and identifies research gaps. It recommends areas where IDRC could best play a role, given its strengths in research and capacity building in light of its current approaches. In particular, this report presents a conceptual framework for PSD support that particularly assists the GGP in the identification of knowledge gaps and research needs, taking account of how PSD is defined and operationalised by researchers, international organisations and donors. It identifies the priority PSD areas of bilateral and multilateral donor agencies, based on their published PSD strategy frameworks and recent consultations. It considers the gaps in knowledge regarding the impact of PSD support and the role of small and medium-sized enterprise (SME) development, suggesting research approaches and topics that would address those gaps. Finally, the

[3] The third theme of the GGP programme initiative is the design and equitable financing of social protection systems.

report identifies indicators that are currently used in the field by different governments and donors for measuring and monitoring PSD impact on pro-poor growth.
This report is organised as follows. The chapter to follow (Chapter 2) examines the purpose of support to PSD. It defines the terms used and identifies the key rationale for support by bilateral and multilateral donor agencies.

Chapter 3 examines the ways in which donor agencies support PSD. This is done by describing the macro, meso and micro-levels of programme intervention, followed by a taxonomy that categorises the technical areas for the support of PSD. Attention is then given to the ways development and donor agencies design, manage and assess their support programmes.

Chapter 4 presents an account of the trends that influence the design and delivery of PSD support interventions. This chapter highlights the emergence of the current approaches to the support of PSD and presents some of the key strategic themes that underpin the support of PSD.

Chapter 5 examines the major debates and controversies that surround the support of PSD. This chapter briefly examines these issues and lays the foundation for the recommendations presented in the chapter that follows. Many of these debates and controversies have been influenced by the recent trends presented in Chapter 4, as well as by evaluations of the effectiveness of PSD support programmes in achieving their anticipated outcomes.

Chapter 6 makes proposals to the IDRC for a PSD research agenda. These proposals are presented in two categories, broadly reflecting the relevant themes of GGP. The first deals with research proposals that deal with the conceptual framework for support of PSD. The second deals with research into the key functional areas for support of PSD.

Wherever possible, this report has drawn on empirical evidence that has emerged from programme evaluations and critiques, and has drawn from a range of policy documents and high-level guidance provided to development and donor agencies engaged in support of PSD in developing and transition countries. While about one hundred documents have been reviewed for this study, it is clear that there are still significant gaps remaining in the literature concerning some of the major assumptions that influence the support of PSD.

While there are ideological paradigms underpinning the various discourses surrounding the support of PSD, this report focuses on the challenges facing policymakers and programme managers. Research topics are identified based on the evidence emerging from the support of PSD and the critiques and current guidance that stem from these findings. The theoretical concepts surrounding the role of the private sector in development, the role of the state and the role of external agencies' support of PSD are better assigned to the specific research activities that follow this report.

2. The Purpose of Support to Private Sector Development

This chapter examines the reasons why international development and donor agencies support PSD. It does this firstly by defining the terms 'private sector', 'private sector development' and 'private sector development support', and then by considering the rationale development and donor agencies use for providing this support.

2.1. The 'private sector' and 'private sector development' defined

Most development and donor agencies define the private sector in similar terms. However, the variations that exist display a potential difference in the approaches used to support PSD. The Canadian International Development Agency (CIDA), for example, defines the private sector as "a basic organising principle for economic activity in a market-based economy where physical and financial capital is generally privately owned; markets, competition, and profit drive allocation and production; and decisions are made and risks are taken as a result of private initiative" (CIDA, 2003, 1).

The Australian Government's Overseas Aid Programme defines the private sector in developing and transition countries with stronger emphasis on the firm, i.e., "a range of privately owned commercial enterprises" (AusAID 2000), including:

- Large multinational corporations whose local enterprises may be a small part of their worldwide operations;
- Joint ventures between foreign-owned companies and local counterparts;
- Large locally owned businesses, such as those resulting from the privatisation of state-owned enterprises; and
- SMEs employing some non-family members, and micro-enterprises, typically consisting of one to three people — often family members and often female – engaging in activities such as farming, handicraft production, street trading, services or small-scale manufacturing.

Recognising the private sector has both international and domestic forms, the United Nations Development Programme (UNDP) places its emphasis on the private sector in developing and transition countries. Accordingly, the role of the firm as an investor is emphasised along with the role the firm can play in economic growth.

> We focus here on the domestic private sector – for three main reasons. First, domestic resources are much larger than actual or potential external resources […] Second, when informal resources are examined, such as the potential value of land, the domestic assets that can be tapped are significantly larger than the cumulative FDI or private portfolio flows. Third, unleashing the domestic resources in an economy – both financial and entrepreneurial – is likely to create a more stable and sustainable pattern of growth (Commission on the Private Sector and Development 2004).

Finally, Sinha, *et al.* defines the private business sector as "a basic organising principle for economic activity where private ownership is an important factor, where markets and competition drive production (and distribution) and where private initiative and risk taking set activities in motion" (Sinha, *et al.* 2001, 18).

As outlined later in this document, there appears to be value in focusing on the systems in which the private sector operates. This focus influences the ways in which the private sector is defined and the support offered to PSD. It is proposed that a systemic understanding of the private sector – one that recognises the role of the private sector to distribute resources within an open market – is most useful. While specific forms of enterprises (such as foreign or domestic firms, firms of different sizes and in different sectors and locations) are useful to identify for the purposes of programme planning, a conceptual framework requires an understanding of these firms operating within an entire sector – the private sector.

PSD in this context has a specific meaning. The World Bank (WB) described PSD as following: "Promoting growth, reducing poverty and helping people improve their quality of life. It is a way of doing things across sectors. Private initiative, unleashed in competitive markets, is key to promoting growth and poverty reduction, in parallel with public sector efforts[…]" (WB 2002b).

Sinha, *et al*. defined PSD as "the process by which the private business sector moves along the path to becoming well functioning" and 'PSD support' as "interventions aimed at developing factors crucial to the development of a well-functioning private business sector" (Sinha, *et al.* 2001, 18).

For the purposes of this report, the latter definitions are the most useful. PSD enhances the functioning of the private sector so that it is better able to contribute to the social and economic development of the country. However, the focus of this report is on the *support* provided to PSD. Thus, the definition for PSD support applies. International development and donor agencies provide interventions (described in Chapter 3) to address the factors that constrain or enable the private sector to function effectively and contribute to economic growth and poverty reduction.

2.2. The rationale: the link between private sector development and economic growth and poverty reduction

Poverty reduction is the primary concern for most development and donor agencies working in developing countries. It is for this reason that agencies are interested in strategies that promote growth and enhance the contribution the private sector can make to growth. PSD is supported through measures that specifically promote the development of indigenous enterprises, as well as through broader measures aimed at improving physical and institutional infrastructure and the mobilisation of private investment for development from both foreign and domestic sources.

For most development and donor agencies, the Millennium Development Goals (MDGs) represent the main focus of their work. The MDGs were adopted by 189 nations and signed by 146 heads of state in September 2000. They “are the first international goals to recognise, at the highest political levels, that poverty in the poorest countries can be dramatically reduced only if developing countries put well designed and well implemented plans in place to reduce poverty – and only if rich countries match their efforts with substantial increases in support” (United Nations Millennium Project 2005, 4).

The MDGs provide shared goals for development and donor agencies and their programme partners. Building on this common platform, the need for coordination and harmonisation became apparent and, in March 2005, the ministers of developed and developing countries responsible for promoting development and heads of multilateral and bilateral development institutions resolved to take ‘far-reaching and monitorable actions’ to reform the ways official development assistance (ODA) is delivered and managed. In what is known as the *Paris Declaration on Aid Effectiveness; Ownership, Harmonisation, Alignment, Results and Mutual Accountability*, these parties recognised that while the volumes of aid and other development resources must increase to achieve these goals, aid effectiveness must increase significantly as well to support partner country efforts to strengthen governance and improve development performance. These changes are necessary to “increase the impact aid has in reducing poverty and inequality, increasing growth, building capacity and accelerating achievement of the MDGs” (OECD 2005b, 1).

Improving aid effectiveness and coordination has required an alignment between international and national development goals, as well as among international development and donor agencies and their partners. It has also led to a review of the kinds of resources that are required to meet the MDGs. The United Nations’ Monterrey Consensus indicates that “a substantial increase in ODA and other resources will be required if developing countries are to achieve the internationally agreed development goals and objectives, including those contained in the Millennium Declaration" (United Nations 2002, para. 41). Private international capital flows, says the Monterrey Consensus, are "vital complements to national and international development efforts" (United Nations 2002, para. 20) and ODA "plays an essential role as a complement to other sources of financing for development, especially in those countries with the least capacity to attract private direct investment" (United Nations 2002, para. 39). As a result, the mobilisation of private investment through the development of the private sector has become a key focus for ODA – including the guidance that development and donor agencies should pay greater attention to domestic investors, both formal and informal, who are the source of the bulk of investment in developing countries (OECD 2006).

Thus, PSD has a strong link with the mobilisation of domestic private investment, which contributes to the promotion of vigorous and sustained economic growth. "Increasing the flow of development aid and reforming the global trading system to provide fair economic opportunities to producers from developing countries are essential for promoting rapid growth in domestic private investment" (Commission on the Private Sector and Development 2004, 2). However, the role of ODA in stimulating investment and fostering economic growth has not been straightforward. Dollar and Easterly found that the links between aid, investment and growth are tenuous: "Aid does not necessarily finance investment and investment does not necessarily promote growth" (Dollar and Easterly 1999, 23). Aid is not the main determinant for investment and growth and there appears to be a number of links between these domains that influence the impact of aid on investment and growth. The first of these is the economic policies established by governments. The second is the poor quality of public services, closed trade regimes, financial repression, and macroeconomic mismanagement. Thirdly, foreign aid cannot easily promote lasting policy reform in countries where there is not a strong domestic movement in that direction.

While these findings may appear to argue against directing ODA towards better investment and growth, they in fact show that the good mix of private investment, policies, and foreign aid is quite important and that disbursing aid into good policy environments would be an improvement on current aid allocations. Burnside and Dollar (2004) argue that donors should focus on the policy and institutional determinants of investment and growth when designing their interventions. Indeed, a robust conclusion from a number of studies covering a diverse sample of countries is that “aid is effective in promoting growth and, by implication, in poverty reduction” (McGillivray 2003).

Support of PSD has been an important ingredient in development and donor agencies’ strategies to boost growth. In 1995, the OECD’s Donor Assistance Committee (DAC) asserted that PSD “promotes efficient economic growth and development and is a source of wealth, dynamism, competitiveness and knowledge” (OECD 1995). Furthermore, the OECD argued that support of PSD “leads to more equitable diffusion of the benefits of growth” (OECD 1995). In the case of micro-enterprises, “these factors are further enhanced by virtue of their particularly direct impact on poverty alleviation” (OECD 1995). Moreover, the more efficient resource use stimulated by PSD creates a larger and more sustainable tax base that can provide the resources for improved social development (OECD 1995).

The United Kingdom’s Department for International Development (DFID) argues economic growth is a “powerful driver of sustained poverty reduction. Vigorous growth and private sector development is strongly associated with poverty reduction, while rising levels of productivity are likely to enhance living standards” (DFID 2000, 2). Moreover, the WB claims that PSD and investment is crucial to spurring economic growth and reducing absolute poverty. Combined with public sector efforts, private investment, particularly in competitive markets, has great potential to contribute to growth. Private markets function as the engine of economic growth, creating productive jobs and higher incomes. With the government playing a complimentary role of regulation, funding, and provision of services, private initiative and investment can help provide the basic services and conditions that empower the poor by improving health, education and infrastructure (WB 2005b, 273). While support of PSD is seen as affecting the performance of the firm (i.e., the successful establishment and expansion of micro, small and medium-sized enterprises), it also has a broader effect on the sector in which these firms operate. The combined effect of improved firm performance (i.e., increasing competitiveness) is felt across the sector and the broader economy. The role of the businessman or woman and the firm in which he or she works is multiplied across the sector, enhancing the growth of local and national economies.

The United Kingdom's DFID says that economic growth is the single most powerful means of decreasing poverty, if the opportunities are available equitably:

> It creates employment and provides higher incomes. Families have more to spend on food and shelter, and people can save, invest and provide for themselves when times are hard. Higher family incomes mean children can go to school rather than having to work. And as economies grow, governments can raise the revenue they need for public services. […]
>
> It is principally the private sector, from farmers and street traders to national and foreign investors, that creates economic growth. Growth is fuelled by the creativity and enterprise of workers and entrepreneurs, which requires the learning of new skills and making the best use of land, minerals and natural resources. It involves taking risks to invest in new ventures that will raise productivity, open up new opportunities and generate tax income for the state (DFID 2007, 35-36).

In Africa, there is growing evidence that the main reason for slow growth and the lack of industrialisation is because of the absence of the private sector, especially the manufacturing sector (Bloom and Sachs 1998, Collier and Gunning 1999a, 1999b, Easterly and Levine 1997, Jenkins and Thomas 1999, Temple 1999). The *World Development Indicators* report for 2007 states that cumbersome business environments hamper growth. "The cost of starting a private business, as a percentage of per capita income, is an indicator of the opportunity for entrepreneurs to develop new economic activities and to compete with existing businesses, an important force driving economic growth" (WB 2007b, 3). This view is supported by the *2005 World Development Report* (WB 2004a), the Commission for Africa (2005), and the series of *Doing Business* reports (WB 2004b, 2005a, 2006, 2007a).

The first MDG, to reduce by half the proportion of people living on less than a dollar a day, is a key target for global poverty reduction. In his 2007 report on progress with the MDGs, the United Nations (UN) Secretary-General claims that the proportion of people living in extreme poverty fell from nearly a third to less than one fifth between 1990 and 2004. If the trend is sustained, the MDG poverty reduction target will be met in most regions. However, it is clear that progress has been uneven. "The benefits of economic growth in the developing world have been unequally shared, both within and among countries" (UN 2007, 8).

PSD is supported by international development and donor agencies in order to promote economic growth that leads to poverty reduction. However, there are increasing concerns that while economic growth may occur, the extent to which the support of PSD has contributed is unclear. This issue will be addressed later in this report. If, the assumption is made that support of PSD contributes to economic growth, then there are additional concerns as to whether this growth leads to poverty reduction.[4] This concern is critical because support of PSD has been justified on the basis of its contribution to growth and poverty reduction, as the following examples illustrate.

The UNDP's Commission on the Private Sector and Development (2004) suggests that in addition to contributing to economic growth, PSD empowers poor people by providing them with services and consumer products, increasing choices and reducing prices.[5] The Asian Development Bank (2000) says that, in addition to contributing to economic growth, PSD can affect poverty in other ways: private investment in infrastructure projects can relieve pressure on public budgets and enable governments to redirect more resources to social spending; and private sector participation in infrastructure can also improve the delivery efficiency of essential services and extend these to the poor. The Inter-American Development Bank supports PSD because of the threefold benefits that stem from private participation in achieving development goals: the enhanced efficiency and coverage that result from the private delivery of goods and services; the use of the private sector to produce services on behalf of the public sector; and the role of the private sector as a partner in socially and environmentally responsible development (Inter-American Development Bank *et al.* 2004). Finally, the main purpose of the Swedish International Development Agency's (Sida) support to PSD is to

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[4] The responsiveness of poverty to growth depends on the distribution of income (or consumption) and how it changes. Many factors influence how the benefits of growth are shared: health, education, infrastructure, gender parity, social safety nets, rule of law, political voice and participation, and access to markets, technology, information, and credit (WB 2005c).

[5] This view is supported by a range of agencies, including the WB (2002b).

contribute to sustainable poverty-reducing growth based on three elements: (i) direct inclusion of the poor in economic activities, contributing to their employment, income and productivity, and to reducing their vulnerability, (ii) economic growth as the means of generating resources in society and enhancing productivity, employment and income, and (iii) redistribution so that the resources generated in society from growth are invested meaningfully for the poor, especially in human resource development.

To conclude, the private sector is a basic organising principle for economic activity. It represents privately owned firms that operate in conditions in which markets and competition drive production and distribution and where private initiative and risk taking set activities in motion. PSD is a process of addressing the constraints and opportunities that influence the growth of the private sector. PSD can also improve the lives of all citizens, including the poor, through the provision of goods and services.

International development and donor agencies support PSD to enhance its contribution to economic growth and poverty reduction. However, support to PSD is also provided to improve the access poor women and men have to services and consumer products, increasing choices and reducing prices. As discussed further in Chapter 5, support of PSD has two broad justifications. The first is to contribute to the growth of the economy – and thereby the reduction of poverty. The second is to contribute to the patterns of growth. Poor women and men are enabled by a more developed private sector through better access to goods and services, and greater opportunities to participate in the mainstream of the economy.

3. Modalities of Support to Private Sector Development

This chapter examines the ways bilateral and multilateral agencies support PSD in developing countries. Attention is given to the general levels and technical areas in which development and donor agencies operate. Across these levels and areas, many instruments are used (e.g., technical assistance, loans, grants, equity finance, capacity building, awareness raising). These instruments are too numerous to present in a report of this nature without simply briefly describing them. Instead, the focus of this chapter is on the strategic areas in which development and donor agencies locate their PSD support interventions.

The chapter is comprised of three sections. The first deals with the levels of support of PSD and the shifts that have occurred in development and donor agency support across these levels. The second section presents a taxonomy of PSD support that categorises key technical areas and reports on the emphasis development and donor agencies assign these. The third section considers the issue of programme assessment and impact.

This chapter sets a framework for the issues that are discussed in the chapters that follow. Some of the major issues of this report are only briefly introduced here and expanded upon in Chapters 4 and 5.

3.1. Levels of support of PSD

The OECD (2005a) describes the roles development and donor agencies can play in influencing the key determinants for mobilising private investment for growth and poverty reduction through activities at the ‘macro’, ‘meso’ and ‘micro’ levels. In each of these domains, a wide range of aid instruments is used, including grants, concessional and non-concessional loans, equity stakes, guarantees, debt relief and technical co-operation.

At the ‘macro’ level, macroeconomic stability and debt sustainability are considered fundamental for promoting economic growth. International financial institutions in particular were found to be working with developing countries in these domains. Similarly, efforts in a variety of areas where DAC members are more substantially engaged (e.g. peace and security, market access and health and education) are of broad relevance for development and their impact goes well beyond that of mobilising investment and support of PSD.

The ‘meso’ level was described as critical in providing an enabling environment for mobilising investment and a domain in which both bilateral and multilateral are active. Working with the relevant policy communities, development and donor agencies support improvements to the regulatory framework (e.g. investment legislation, competition policies, tax policies, trade policies and financial markets), governance and infrastructure.[6]

While improvements to the investment climate and business environment help to mobilise investment, this alone is not sufficient to maximise the investment potential in developing countries. For this reason, development agencies also work at the ‘micro’ level, to ”strengthen the ability of enterprises in developing countries to respond to the lowered trade barriers and new opportunities arising from a better enabling environment and greater international integration" (OECD 2005a, 14). These activities include investment promotion and facilitation, promotion of business partnerships between firms in industrialised and developing countries and support for the development of local businesses.

Further details on the macro, meso and micro level interventions are presented in Figure 1. This figure locates a range of technical areas that can be found across the three levels of PSD support.

Figure 1: Overview of levels and intervention and relevant technical areas

Level of intervention	Technical areas
Macro-level interventions	Macro-economic stability Budget and financial management, including debt stability Open and competitive markets Investment climate reforms

[6] Also see OECD (2004b).

Level of intervention	Technical areas
Meso-level interventions	Business environment reforms, including: • Policy, legal and regulatory framework, such as: - Privatisation policies and programmes - Investment policies and laws - Taxation - Labour policies, laws and regulations - Competition laws - De-regulation/re-regulation and administrative reform • Legal and institutional reform, including: - Rule of law - Contracts and commercial dispute resolution - Property rights • Organisational development, such as business membership organisations • Public-private dialogue • Public and corporate governance • Trade capacity building and facilitation, including: - Strengthening trade-related institutions - Support in trade negotiations Financial services and financial sector reform Restructuring of state-enterprises Infrastructure and utilities development and management
Micro-level interventions	Investment promotion Entrepreneurship promotion Micro, small and medium enterprise development Value chains and clustering Business-to-business linkages

As explained in the chapter that follows, most agencies are shifting their interventions away from the micro-level and more toward the meso. This has largely been due to the increasing pressure on agencies to expand the impact PSD support has on PSD, growth and poverty reduction. Those agencies that continue to support micro-level interventions displayed a change in their approach, such as using more market-oriented strategies.

3.2. Technical areas of multilateral and bilateral PSD support

In one of the first major comparative studies on bilateral and multilateral donor agency support for PSD, Schulpen and Gibbon (2002) found a great deal of similarity, with the only major difference being in the modalities used: multilateral donors were more engaged in lending.[7] However, they found that, aside from lending for structural adjustment and the privatisation of state-owned enterprises, the most frequently encountered form of PSD assistance was direct support to enterprises.

Both multilateral and bilateral agencies were found to apply a ‘one size fits all’ model in which the environment for PSD plays a central role. Both displayed a strong preference for instruments and programmes at the macro and micro-levels, with a wide overlap in programmes and instruments being found. Overall, the authors found high levels of competition between donor agencies and poor coordination; they argued that the poverty reduction strategies and planning frameworks offer a route “out of this maze, but probably this will be taken only by countries applying for HIPC relief” (Schulpen and Gibbon 2002, 26).

In a recent global review of PSD support provided by bilateral and multilateral agencies for the Private Sector Division of the UNDP, Habib and White (2007) applied the following taxonomy of PSD support activities (See Figure 2). Three broad categories of PSD support were defined, each with its own technical area. These categories of support largely fall within the micro and meso levels outlined above. While there are significant overlaps between the technical categories, as well as some omissions, this taxonomy and the results of the agency survey provide a better understanding of how development and donor agencies provide support of PSD.

[7] For example: World Bank, African Development Bank, Asian Development Bank.

Figure 2: Taxonomy of PSD support

PSD Category	Technical Area	
PSD 1: Enabling Environment	1	Policy Dialogue and Policy Formulation
	2	Business Environment Reform
PSD 2: Access to Skills, Knowledge and Capital	3	Entrepreneurship Promotion
	4	Business Development Services
	5	Access to Finance
PSD 3: Access to Markets and Market Facilitation	6	Supply and Value Chain Development
	7	SME Clustering
	8	Trade Facilitation and Support for Global Competitiveness
	9	Investment Promotion
	10	Privatisation and Enterprise Restructuring
	11	Making Markets Work for the Poor
	12	Sector Wide Approaches

SOURCE: Adapted from Habib and White (2007)

PSD 1: Enabling Environment

This PSD category consists of two technical areas of PSD support:

1. Policy Dialogue and Formulation: Technical assistance and capacity building support for the development of national PSD support policies, including interventions to increase policy dialogue between business and government and the establishment of national business councils.
2. Business Environment Reform: Interventions aimed at reforming laws and regulations that set the 'rules of the game' for businesses and reduce unnecessary obstacles to doing business, typically business registration procedures, licenses, permits, inspection regimes, customs, tax and tax administration systems.

PSD 2: Access to Skills Knowledge and Capital

This PSD category consists of the following technical areas of PSD support:

3. Entrepreneurship Promotion: Interventions to promote entrepreneurship and the development of entrepreneurship skills (e.g., education programmes, youth

entrepreneurship initiatives, vocational education and training schemes, and support for the establishment of specialist business schools).

4. Business Development Services: Interventions aimed at increasing the supply of counselling, consultancy and advisory services that assist businesses to achieve profitability and growth (e.g., the establishment of national and local enterprise support agencies, business incubators, capacity building support for business representative organisations, business associations and embedded service suppliers).
5. Inclusive Financial Sectors and Access to Finance: Support for the development of financial services to support micro-enterprises, SMEs and poor consumers (e.g., micro-credit, micro leasing, guarantee funds, specialised SME credit lines, venture capital, private equity, factoring, and consumer finance).

PSD3: Access to Markets and Market Facilitation

This PSD category consists of the following technical areas of PSD support:

6. Supply and Value Chain Development: Interventions aimed at facilitating market linkages for local producers and identifying and addressing value chain bottlenecks (e.g., information asymmetries, regulatory barriers and their enforcement, administrative barriers, market structures and competition policy, tariff and non-tariff barriers to trade, infrastructure deficits, factor price rigidities, price restrictions and subsidies). It includes value chain studies and initiatives for awareness raising and matching, support for 'spillovers' from lead businesses, the promulgation of generic and sector specific standards, the establishment of standards infrastructure, quality assurance, franchise development, and specific supporting activities for pro-poor value chains (especially in agriculture).
7. SME Clustering: Spatial or area-based initiatives designed to facilitate economies of agglomeration and promote the development of 'growth poles' (e.g., science and technology parks, local sourcing agreements).
8. Support for Global Competitiveness and Trade Facilitation: Interventions aimed at increasing the international competitiveness of local producers and enhancing their readiness and ability to compete in international markets (e.g., competitiveness benchmarking, support for the attainment of international, support for the

establishment of sectoral business associations, institutional strengthening initiatives for chambers of commerce, export associations and support agencies, export credit funds, and business-to-business linkages.

9. Investment Promotion: Interventions aimed at identifying sources of local comparative advantage and strengthening the ability of beneficiary countries and regions to attract and retain of foreign direct investment (e.g., investment benchmarking studies, place marketing, the establishment and networking of investment promotion agencies).
10. Privatisation and Enterprise Restructuring: Support for government privatisation strategies and direct enterprise support for the restructuring and privatisation of state owned enterprises, including post privatisation assistance ('turn around' management) and appropriate social mitigation measures (e.g., the provision of vocational education and training, and entrepreneurship training).
11. Making Markets Work for the Poor: Systemic approaches to private market development designed to improve the functioning and outreach of markets, rather than enterprises.
12. Sector Wide Approaches (SWAps): Coordinated multi-donor initiatives based on government led sector development programmes.

Habib and White (2007) surveyed ten bilateral and multilateral agencies, as well as the global network of UNDP offices engaged in support of PSD and found PSD Category 1 (Enabling Environment) was the top of the donor agenda with its technical areas ranking first and second. This is followed by Access to Finance (PSD 2), then Supply Chain Development (PSD 3) and Trade Facilitation (PSD 3). This was believed to reflect the current trend toward a more systemic approach to support of PSD, where the external environment and the role of markets are considered important influences on the establishment and development of private enterprises. There was a greater focus on enabling policies and the removal of regulatory barriers to create a conducive environment in which the private sector can grow. Receiving low priority scores were the four technical areas from PSD 3: Investment Promotion, SME Clustering, PSD Sector Wide Approaches, and Privatisation and Enterprise Restructuring. An additional, low scoring technical area is Active Labour Market Measures (PSD 2).

Thus, development and donor agencies spread their support for PSD across the three macro, meso and micro levels. Macro level interventions are more focused on broad investment climate issues and have less of a focus on PSD. Meso-level interventions on the other hand have become much more aligned with PSD support issues. The promotion of markets and the assessment of the broader system (i.e., institutional and cultural systems) have become much more central to the support of PSD in developing and transition countries.

Schulpen and Gibbon (2002) describe a 'division of labour' where multilaterals were providing the greater part of macro-level reform support and bilaterals were largely marginal in this field. This is consistent with the finding of White and Chacaltana (2002) who noted that many developing-country governments were more comfortable working with multilateral donor agencies on these issues because these agencies are considered to be more neutral. Bilateral donors, on the other hand, usually have the interests of their own country. While these interests may be well intended or benign, host governments recognise that bilateral donor agencies are instruments for trade, security, and other political agendas of donor governments. Opening up domestic reform issues to foreign governments can place host governments in a position of vulnerability – whether perceived or real.

As will be shown in the following chapter, new areas of meso-level reform and development have emerged in recent years. This includes the role of public-private dialogue and support for improved corporate governance. While there has been a shift in PSD support activity towards the meso-level, many development and donor agencies still support micro level reform, but to a much lesser extent. Many bilateral donor agencies continue to support donor country investments or exports and business-to-business twinning arrangements. Greater attention has also been given to value chain development and the development of markets for business development services. Many of these trends are presented in more detail in the following chapter.

3.3. Programme monitoring and evaluation, and impact assessment

International development and donor agencies have become increasingly concerned with the inadequacies of research on programme evaluation and impact assessment. Assessing the impact of PSD on firms is critical for development and donor agencies that have to explain the use of resources on these programmes. This challenge becomes even greater when the contribution PSD support has on economic growth and poverty reduction are examined.

Many donor and development agencies surveyed by the UNDP (Habib and White 2007) indicated that, while the monitoring and evaluation of PSD support programmes is a relatively straight forward and institutionally entrenched activity, impact assessment remains a significant challenge. Most agencies reviewed use evaluators or assessors who were removed from the programme itself and there appears to be a growing trend in using external evaluators. These external evaluators may be from completely independent agencies, such as independent evaluation firms or from evaluation units that have been set up within the agency.

There are two broad areas of concern within the field of programme monitoring and evaluation, and the measurement of the impact of PSD on the achievement of broader development goals. The first of these deals with impact and the extent to which donor and development agency interventions actually contribute to economic growth and poverty reduction. The second deals with programme performance and the causal links between programme outputs, outcomes and impact.

At the broadest conceptual area, there are concerns as to how PSD contributes to growth and to the reduction of poverty in developing economies. In 2000, the International Finance Corporation produced, *Paths out of poverty; the role of private enterprise in developing countries*, in which the importance of economic growth through PSD was elaborated: “growth is the surest way to achieve upward mobility and poverty reduction, as well as to secure financing for health and educational programs and other initiatives directed toward poor people” (International Finance Corporation 2000, 25).

This work highlighted the results of a wide range of PSD studies and identified areas in which PSD could be enhanced to produce growth and poverty reduction. The WB's study, *Voices of the Poor*, found that next to illness and injury, the scope for entrepreneurial activity and the availability of jobs is the most important factor determining the fate of poor people (Deepa 2000).

Ravallion and Chen (2001) raise the concern that improvements in economic growth, whether through PSD or as a consequence of any other intervention or change, are not necessarily equally distributed and that pro-poor outcomes cannot always be assumed. They argue for a better measure of pro-poor growth, referred to as the 'mean growth rate of the poor', which can be derived from a 'growth incidence curve' giving rates of growth by quintiles of the distribution of income.

Much of the assessment undertaken at this level is with the aggregate performance of the economy as a whole, with particular attention given to the role of the private sector in the economy, and to how the benefits of economic growth are distributed. This typically involves the analysis of macroeconomic indicators. However, efforts have also been made to assess the impact of specific policies, programmes and institutions within the overall framework. Strategic-level impact assessments have been used to improve the quality of policy design and the effectiveness of their implementation. There is growing use of strategic impact assessment to assess the economic, social and environmental impacts of trade policy in developing countries, as well as the impact of regulatory change (George and Kirkpatrick 2003b).

Causal chain analysis has been used to identify the significant cause-effect links between a proposed policy change and its eventual impacts (i.e., its impact on economic growth and poverty reduction). The aim of this approach is to distinguish the significant cause-effect links in the chain. Significance criteria have to be formulated and then used to eliminate non-significant sections and terminate further analysis beyond these sections. The analysis is usually undertaken, in logical sequence by section, from 'cause' to 'effect'. Causal chain analysis of a single policy can be extended and considered in a broader context. It can be used to assess a comprehensive approach to poverty reduction, such those contained in Poverty Reduction Strategy Papers by considering the aggregate cause-effect linkages (George and Kirkpatrick 2003a).

The second area of interest in programme monitoring, evaluation and impact concerns the performance of donor-support PSD programmes and the extent of their contribution to improving the performance of the private sector. Assessing the impact of micro-level interventions, such as Business Development Services (BDS) is concerned with assessing the impact of BDS on private enterprise clients, such as changes in enterprise performance (e.g., sales, value added, profitability) or broader social and economic impact (e.g., employment, poverty alleviation). In most cases, this is the most critical form of assessment. With all the effort and attention given to designing and delivering BDS interventions, development and donor agents want to know if there has been an impact on the enterprise sector. There are many problems experienced when undertaking assessments of this kind, including the problem of the counter-factual.[8]

Honest evaluations of BDS programmes revealed that most programmes reached only three to four percent of the total target group. The remaining 96-97 percent went without this support. Furthermore, there were serious questions raised about the overall impact of subsidised BDS (i.e., where BDS is provided to a small enterprise for free or at a cost lower than what would make the service feasible). Attempts to answer these questions brought BDS practitioners to the inevitable topic of the markets in which BDS operate.

One of the greatest challenges for agencies is to become clearer about the causal links between BDS, improvements in business performance, and the achievement of a broader development objective (e.g., job creation, poverty reduction, economic growth).

[8] Attribution refers to the problem of isolating a BDS and showing that it was the sole reason for an improvement in small enterprise performance. Advice in business planning may have helped the business owner to organize her business better and plan for expansion, but how can we be sure that this alone led to the increase in annual turnover? The problem of the counter-factual is a hypothetical one. What would have happened without the BDS? If the business owner did not get advice on business planning, does that mean her business would not have grown? Would it have grown less? Would it have grown more if the advice had been better, more intensive, longer?

This requires programme managers to be clear about the purpose of their interventions and the way they measure change (see Oldsman 2003, Oldsman and Halberg 2002).

A noteworthy innovation in impact assessment comes from Nadvi and Barrientos's (2004) study for United Nations Industrial Development Organisation (UNIDO), which seeks to understand the effects of industrial clusters on poverty reduction. Their approach combines quantitative and qualitative approaches to value-chain mapping and capabilities assessment, focused on understanding the capabilities of the poor. Investigating the poverty level of different groups within value chain maps helps identify poverty nodes where poorer groups are located within a cluster. This helps to assess the impact on poverty based on different categories of firms and workers and identifies differences in poverty impacts based on gender, ethnicity and religion. Another recent example is the Method for Impact Assessment of Poverty Alleviation Projects (MAPP), which applies qualitative and participatory methods using stakeholder workshops. MAPP assesses whether poverty-reducing processes actually occurred in a project by understanding the perspectives and behaviour changes of those in the causal chain (German Development Institute 2004).

Effective impact assessment of business environment reform programmes draws evaluators back to the strategic level impact assessments and causal chain analysis referred to above. These assessments should allow for the assessment of reform interventions in terms of their outcomes and final impacts of the intervention. There are four stages involved in doing this (Pinder 2005, Pinder *et al.* 2005):

- Stage 1 involves initial screening: Screening the conditions for private sector development and the country context. This is a scan across the range of policies, regulations and institutions affecting private investment to identify constraints to domestic and foreign investment and identify areas of focus for reform.
- Stage 2 is an ex ante appraisal: A review of the key conditions for private sector development and an assessment the ways the proposed programme will affect the conditions for private sector development and the achievement of broader development objectives (e.g., pro-poor growth).

- Stage 3 involves regular monitoring and evaluation that is built into programme design and implementation to ensure there is timely feedback on outcomes and impact from the start.
- Stage 4 is an ex post evaluation that is conducted to assess the actual impacts of the intervention against the baseline scenarios developed at ex ante stage.

The process of measuring the impact of donor-supported business environment reforms should involve a partnership between the donor and development agency, the government and the private sector. Together, these parties can explore the constraints on enterprise activity and its impact on pro-poor growth.

4. Trends and Patterns in PSD Support

This chapter briefly surveys some of the major trends in the provision of support to PSD in the last twenty years. It focuses on the highlights within these overall trends in order to identify some of the conceptual shifts in approach over this time. These trends help us to better understand the emerging areas of policy and practice that shape support of PSD and lead toward the identification of the gaps in knowledge in this field.

4.1. The separation of financial and non-financial services

In the 1970s and early-1980s, financial and non-financial services were combined in integrated business development programmes. However, in the late-1980s and early-1990s, there was a separation of financial and non-financial services in an effort to achieve greater sustainability through specialisation.[9] Financial services referred to the range of financial mechanisms that are used to help enterprises start-up and expand (e.g., loans, banking services, revolving funds, microfinance). In the early 1990s, the

[9] This long-time separation between BDS and financial services has recently been contested. There is growing evidence of improvements gained through a more integrated approach (see Sievers and Vandenburg 2004).

Consultative Group to Assist the Poor (CGAP), a consortium of 33 public and private development agencies, was formed to help build inclusive financial systems that serve the poor, with a particular emphasis on building local, deposit-driven markets. The CGAP strategy focuses on ensuring local financial markets are equitable and efficient, and that finance for the poor is fully integrated into mainstream markets.[10]

In 1997, the international Committee of Donors for Small Enterprise Development coined the term 'business development services' (BDS) in preference to the term 'non-financial services'.[11] BDS was defined as:

> Services that improve the performance of the enterprise, its access to markets and its ability to compete. [This includes] a wide array of business services, both strategic and operational. BDS are designed to serve individual businesses, as opposed to the larger business community (Committee of Donor Agencies for Small Enterprise Development 1997).

BDS has come to embrace micro-level development instruments such as management training, counselling and advice, developing commercial entities, technology development and transfer, information, and business linkages.

4.2. The move 'up-stream'

Many development and donor agencies engaged in support of PSD suggest that their work over the last ten years has moved 'up-stream'. Where once agencies and their programme partners (i.e., in the past, the main programme partner was government) focused on the provision of services directly to nascent or expanding enterprises, the focus has become much broader. Along with this trend, bilateral and multilateral agencies have worked with a wider range of programme partners.

The move up-stream, as well as toward a more market-based and systemic approaches (see 4.3 and 4.4, below), progressed from the Sustainable Livelihoods Framework established in the late 1990's. This approach identified the ways in which poor people

[10] For more information, see http://www.cgap.org .

[11] Since 2005, this agency has been renamed the Donor Committee for Enterprise Development.

accessed the products and services they required and examined the transaction costs associated with this access.

The first shift from focusing directly on enterprises was a move toward support for intermediary organisations that could provide development services to firms in a more business-like and commercially oriented manner. This brought development agencies in greater contact with non-government and community-based organisations, business membership organisations, and privately owned businesses. However, the shift continued to broaden to include work at the policy level. Here government was again a primary programme partner, but other partners were also brought into this engagement (e.g., local universities, consultancy firms, business membership organisations). This 'up-stream' work required development and donor agencies to apply a new set of skills related to the policy domain (e.g., policy assessment, policy writing), which for some agencies has been a difficult challenge (White 2004). Enterprise development sections of a number of agencies became reorganised into sections dealing with economic development, growth, or sustainable development.

Finally, this 'up-stream' work has moved beyond the domain of policy development. While ministries of trade and industry in developing countries remain key actors in support of PSD, other ministries such as finance, treasury, and economic planning have become more engaged. In addition, the shift toward more market-based and systemic approaches has seen greater levels of engagement with other elements of the state (i.e., parliament, judiciary) and other actors such as regulatory and competition authorities, trade unions, regional economic agencies, and the media.

4.3. Addressing market failure

Failures in PSD have increasingly become recognised as failures of markets. The provision of BDS was defined as a response to the failure of markets in the provision of business services. The Donor Committee on Small Enterprise Development undertook a process in the late 1990s to derive principles of good practice, which culminated in the production of the 2001 Donor Guidelines (otherwise known as the 'Blue Book'). These guidelines gave greater attention to the importance of meso-level organisations, especially to what has been described as ‘BDS organisations’ or more accurately ‘BDS providers’. The market in which BDS are designed and delivered became an important consideration. It became clear that the business services sector was growing around the world as more and more enterprises obtained the services they required from private sources. Moreover, many BDS providers were disconnected from these markets, which was a reason that many BDS programmes failed (Gibson 1999). This introduced a number of new terms to the BDS lexicon, including the ‘market paradigm approach to BDS’ and the ‘BDS facilitator’.

A broader elaboration of this trend has been demonstrated by the emergence of the ‘making markets work for the poor’ approach to PSD. The making markets work for the poor approach moves beyond a focus on business services to the broader range of goods and services required to reduce or alleviate poverty. This includes commodity markets, property markets, labour markets and financial markets. It is based on a set of core principles and interventions. The approach recognises that:

- Poor people are more than mere victims of circumstances. They are also creative individuals who strive to lift themselves out of poverty in a plethora of ways.
- A major barrier preventing people from breaking out of poverty themselves is not their deprivation, or poverty itself, but the problematic environment in which they are forced to pursue their livelihoods.
- An effective approach to help the poor in a sustainable way is to tackle those barriers that stand in the way of their ability to help themselves (e.g., strengthening property rights, improving financial markets, providing infrastructure that will link poor producers to bigger markets or to cheaper goods) (Centre for Development and Enterprise 2006, 21).

Sida claim that if PSD is to make markets work more effectively for the poor, then “close attention has to be paid to the institutional framework and particularly its ability to secure informal property rights and the good management of common resources” (Sida 2003, 28). Thus, the making markets work for the poor approach moves beyond the firm level and the deficits of the firm. It locates the firm (and, indeed, the poor in general) in an institutional framework in which transactions are made to purchase goods and services. Improving the access poor women and men, and the firms they own and manage, have to goods and services of all kinds supports the development of the private sector through market-based measures.

An underlying theme for reforming governance structures, says Holden (2004) is to promote private sector development so that private markets allocate resources in a powerful and efficient way such that all levels of society can benefit from a growing and vibrant private sector. "Competitive markets, by definition, are self-regulating, and government regulation and intervention should be directed toward establishing clearly defined market procedures, ensuring equal access to and open disclosure of information, and facilitating market transactions" (Holden 2006, 6).

Markets are governed by regulations and the institutions that enforce them. The public regulatory system of a country - the collection of public policies, legal instruments, processes and institutions that establish legal constraints on private behaviour - is at the core of its relationship with the economy and society at large. There is no ideal model for the 'right' regulatory system. The precise role that markets and governments can play varies from country to country and from sector to sector. Successful countries show much variation. However, a growing body of literature on the determinants of growth suggests that the state will need to:

- Increase the scope for markets to work efficiently by eliminating state-owned and legal monopolies, barriers to entry and exit such as unnecessary licenses, and other interventions into commercial decisions such as price controls (these simplification, liberalisation, and deregulation policies usually aim to intensify market competition).
- Provide a market framework of policy, regulatory, and judicial functions to protect property rights, promote competition by controlling market abuses, carry out competitive procurement, and provide efficient services to the private sector such as registration, licensing, and a contractual system for economic transactions.
- Expand its attention to social policies such as funding transfer payments that underpin the welfare state, educating, providing health services, financing

universal service programs, and promoting safety, health, environmental quality, energy security, and other objectives that may not be properly valued in the market (these protective and welfare functions of the State are rapidly becoming its core functions) (Jacobs 2005).

These reforms improve private sector performance in two ways. They free up the market and stimulate competition so that enterprises can adapt and innovate more quickly, and they enhance the capacity of the public sector to provide an enabling environment of sound regulation and efficient public services.

Moving to the modern regulatory role of the state is a ‘good governance’ agenda, not a narrow ‘deregulation’ agenda. Regulatory reform is a multifaceted strategy that includes deregulation, re-regulation, simplification and institution-building. Reform can mean revision of a single regulation, scrapping and rebuilding an entire regulatory regime and its institutions, or improvement of processes for making regulations and managing reform. Deregulation is a subset of regulatory reform and refers to complete or partial elimination of regulation in a sector to improve economic performance (OECD 1997).

The role of markets and their importance in economic growth and poverty reduction has brought greater attention to the role of investment in development – and particularly in the role of private investment as compared with public sector investment. As noted previously in this report, the mobilisation of private investment has become recognised as a critical component for development as recently expressed in the Monterrey Consensus (UN 2002). This has led to increasing interest among donor and development agencies in the reform of investment climates and business environments – including the improvements of institutional and physical infrastructure – often considered binding constraints to investment and growth in many developing economies (Kikeri *et al.* 2006).[12] Writing on the private sector in the Pacific, Holden *et al.* claim that countries reduce poverty when they undertake two fundamental actions: “first, building an inviting investment climate in which private entrepreneurs will invest and generate jobs; and

[12] For further information on identifying and addressing the binding constraints to investment and economic growth, see Carlin and Seabright (2007) and Hausmann *et al*. (2005, 2006).

second, investing in the education of people so they can participate in the economic growth generated by private entrepreneurs, and as they learn business practices, become entrepreneurs themselves” (Holden *et al.* 2004, 52-53). The role of investment climate and business environment reform in PSD is described further in sub-section 4.5, below.

4.4. Systemic approaches to PSD

The systemic approach to PSD takes a market-driven strategy further. Rather than targeting one lead firm's supply chain, one set of linkages among cooperatives, one specific cluster, or even one set of vertical linkages among several firms, “market system development strives to achieve a wider set of goals and incorporates a wider set of dimensions in order to generate continuous growth” (Tanburn *et al.* 2006). Within this context, five dimensions to a systemic approach have emerged:

- The context: the cultural, environmental, political, health and other physical and social factors that influence markets and the target population;
- The business environment: the global, national and local government policy and regulatory influences on the market, as well as government services and infrastructure that affect the market;
- Institutions: learning institutes, universities, business membership organisations, research institutes, NGOs and development initiatives that contribute to and influence the market;
- The core market itself: businesses, their associations and input suppliers that take products from raw materials to market, or that create and market services to consumers and other businesses;
- Support markets: technology, business, and financial services that are pivotal to the exchange of goods and services and the strength and dynamism of the market (Tanburn *et al.* 2006, 17-23).

Systemic approaches to PSD support require policy makers and PSD practitioners to locate the private sector within network of institutions that determine the incentives and disincentives for growth and distribution. The firm-level perspective is still important.

Domestic and foreign enterprises remain an important source of information on how the private sector is performing and where the opportunities and constraints lay. However, the response to these issues (e.g., the response to binding administrative constraints and the response to the opportunities created by freer cross-border trade) should be based on a systemic understanding of these issues.

4.5. Better business environments and investment climates

As noted previously, supporting the improvement of the investment climate (macro-level reforms) and the business environment (meso-level reforms) is not new to the work of development and donor agencies. However, greater attention has been given to this issue in recent years.[13]

The *World Development Report 2005* focuses on the role of investment climates for economic growth and poverty reduction: "Improving the investment climate – the opportunities and incentives for firms to invest productively, create jobs, and expand – is the key to sustainable progress in attacking poverty and improving living standards" (WB 2004a, 19). The OECD has recently described work on the business environment as a 'new private sector development agenda'. The new agenda is broader than the old one and moves from directly helping the poor (e.g., to establish their own enterprises or to provide micro-finance programmes), to the development of 'market outcomes that may be more or less pro-poor'. It suggests, therefore, that the focus of donor support should "be on 'institutions and policies that influence market outcomes" (OECD 2004, 9). This focus was confirmed in a the WB Group evaluation of its assistance for improving the investment climate that highlighted the importance of reforms at the institutional level, even more than at the policy level (WB Group, 2004b).

While some development and donor agencies focus their efforts on a narrower range of themes, most appear to agree that improving levels of investment in developing and transition countries requires reforms in a number of areas or development themes (see,

[13] See Commission for Africa (2005), World Bank (2003, 2004a, 2004b, 2005a, 2006, 2007a), White and Chacaltana (2002), and White (2004).

for example, Carlin and Seabright 2007). DFID, for example, states it is increasingly adopting a multidisciplinary approach involving enterprise, economic, governance, livelihoods and infrastructure perspectives (DFID *et al.* 2004). However, development and donor agencies vary in their views on which areas or development themes are the most appropriate or most significant to address when supporting reforms that develop the private sector. For example the WB's Operations Evaluation Department have categorised areas of investment climate reform into 'core' and 'non-core' themes.[14] Core investment climate themes include regulation and competition policy, corporate governance, legal institutions for a market economy, judicial and other dispute resolution mechanisms, and personal and property rights. Non-core themes include tax policy and administration, infrastructure services for private sector development, export development and competitiveness, trade facilitation and market access, and other financial and private sector development (WB Group 2004, 7).

The current draft donor guidance for business environment reform of the Donor Committee for Enterprise Development defines the business environment as "a complex of policy, legal, institutional, and regulatory conditions that govern business activities. It is a sub-set of the investment climate and includes the administration and enforcement mechanisms established to implement government policy, as well as the institutional arrangements that influence the way key actors operate (i.e., government agencies, regulatory authorities, business membership organisations, civil society organisations, trade unions, etc.)" (Committee for Enterprise Development 2007).

Many development and donor agencies attempt to identify the most binding constraints to PSD.[15] Within this context greater attention is being given to regulatory reform and the promotion of competition policies. The DFID/Foreign Investment Advisory Service (FIAS) Better Regulation for Growth (BRG) programme, for example, aims to improve the regulatory dimensions of the business environment to stimulate productive investment by

[14] Government of the Netherlands has proposed that the categories "core" and "non-core" be replaced with "narrow" and "broad" to avoid the implication that one category of activities is more important than the other (Vlaar 2005).

[15] See Hausmann *et al.* (2006)

the private sector, leading to increased economic growth and poverty reduction. The programme helps developing country governments improve their regulatory management, institutions, processes and quality and aims to produce a set of practical policy tools and implementation guidelines to encourage and support systemic regulatory reform efforts in developing countries. The programme deals with three aspects of regulatory reform:

(i) The immediate bottlenecks - the stock of existing regulations;

(ii) The way that government works when considering new policies, laws, regulations and delivery of public functions (i.e., the flow of regulations); and

(iii) The institutions responsible for preparing and vetting draft regulation, and for driving the regulatory reform agenda.

Many of the WB's *Doing Business* indicators have created benchmarks for business environment reform. However, there is growing concern that donor agencies and their programme partners are focusing too much on improving these indicators and not enough on the underlying causes of a poor rating on any or all indicators. The "problems in the business environment are normally systemic" says Channell (2007), they arise from historical reasons, ranging from colonial experience to ideological commitments.[16] Frequently, the original design of the business environments in developing countries was not business friendly: colonial powers created systems that created a few elite "winners" without regard for potential investment by the local population. "These designs were sometimes then made worse through adoption of authoritarian or ideological reforms that concentrated business and trade into an even smaller group of privileged owners, or into the hands of the state, which was unable to run the business effectively. As a result, the business environment may suffer from serious design flaws on a systemic level" (Channell 2007, 4).

International development and donor agencies working in the field of business environment reform are encouraged to adopt a systemic approach to reform. This means they should consider the whole system, including all the relevant institutions, the 'rules of

[16] Also see Bannock (2002).

the game', cultural and social norms and other key elements, such as the existing stock of regulations and the processes of reform in each case.[17] Systemic reform is not a one-off act, but a process of adapting to new challenges and changes. Such reform includes relatively specific or narrowly focused reforms, those that involve a degree of trial and error (e.g., pilot reforms), as well as more comprehensive reforms of a grander scale.

4.6. Responding to a more integrated world economy (trade facilitation)

Increasing levels of integration in the world economy require developing and transition countries to trade internationally within a more open system. Many developing countries face supply-side constraints that severely limit their ability to benefit from the multilateral trading system. DFID argues trade is not currently working for the poor: the world's 49 poorest countries together accounted for 0.4 percent of world trade in 1999 – half of the level of 1979. Thus, the MDGs include a fairer trading and financial system.

During the mid-1990s, trade was not a high priority for development co-operation in many developing countries and transition economies. Bilateral and multilateral agencies put a lower emphasis in their policy analysis and assistance programmes on trade policy reform and trade capacity development in favour of other important elements of the development agenda such as governance, education, health and environment. However, the emergence of a more integrated international trading system poses serious opportunities and challenges for developing countries often currently at the margins of the global economy. This has necessitated a re-think on trade within development cooperation and a particular examination of the relationship between trade, growth and poverty reduction.

One of the international flagships for assistance in this field is the Integrated Framework for Trade Related Technical Assistance to Less Developed Countries. This initiative that brings together bilateral donor organisations and six core multilateral agencies (i.e., the

[17] See Reinprecht (2005) and Kikeri *et al.* (2006) and Organization for Security and Co-operation in Europe (2006).

WB, the International Monetary Fund (IMF), the UNDP, the United Nations Conference on Trade and Development (UNCTAD), the World Trade Organisation (WTO) and the International Trade Centre (ITC)) to better co-ordinate efforts to mainstream trade and build the trade-related capacities of less developed countries. However, there is a range of other initiatives supported by bilateral and multilateral agencies, such as the Aid for Trade initiative. At the recent G8 Summit in Germany, a declaration on Growth and Responsibility in Africa was adopted in which the G8 identified trade as 'a key engine of growth' and committed itself to supporting trade capacity building and the recommendations of the WTO's Aid for Trade Task Force to improve quality and monitor delivery of the commitments on Aid for Trade (see Box 1). In addition, many developed-country governments have introduced bilateral trade agreements and initiatives that promote increased trade with developing countries.

Box 1: Excerpt from the Declaration on Growth and Responsibility in Africa , G8 Summit

"We expect spending on Aid for Trade to increase to US$ 4 billion, including through enhancing the Integrated Framework. We welcome the role of the WTO Secretariat and Director-General, as well as the OECD, in monitoring the delivery of these pledges and ensuring that aid for trade plans in poverty reduction strategies are funded in a coordinated manner." (G8 Summit 2007)

For many international development and donor agencies trade-related capacity building activities have moved from trade-related technical assistance, which focussed on export marketing and trade liberalisation, to trade facilitation (i.e., reducing transaction costs) and promoting awareness and knowledge amongst national institutions of the rules, procedures and institutions of the international trading system. A part of this shift in focus has been the move from a sectoral focus (i.e., working in sectors that showed the most promise for export promotion), to a broader environmental approach and the facilitation of trade. A consequence of this shift has been a change in development partners as well as the scaling up of donor interventions in this field. For example, DFID programmes in this area go beyond the country level, focusing more on working with multilateral agencies (e.g., UNCTAD, ITC, WTO) than in the past (North-South Institute 2004). UNIDO claims that while the development of a private exporting sector, and the development of standardisation, product testing and other conformity assessment capabilities have always been a part of its core mandate, a more systemic approach to trade capacity building have been pursued in the last five years. This work is considered to be a contribution to the PSD 'debate' concerning the need "to strengthen the enabling environment for establishing and proving compliance with market requirements" (United Nations Industrial Development Organisation 2007).[18]

DFID suggests that as well as minimising adverse effects of adjustment costs, trade reforms can also be designed to have a much greater likelihood of transmitting sustainable benefits for poor people. There are many measures that can be used to achieve this objective, but "the key is to ensure policy makers are able to consider poverty impacts up-front at the start of the reform design process" (Pengelly 2001). Thus, the challenge for agencies engaged in the support of PSD is to identify the potential impacts trade-related reforms will have on poor producers (e.g., farmers) as well as the domestic private sector. Efforts are also required to improve the capacity and capabilities of key developing-country agencies to effectively engage in trade negotiations and to provide an effective national policy response to these issues.

4.7. Support of business membership organisations

The term 'business membership organisation' (BMO) is used to describe a wide range of organisations that are formed by business and in the interests of the business sector they represent. BMOs can also be known as small business associations or chambers of

[18] Brief notes on the debate: While the integration of global markets may not be a bad thing, globalisation can, say Rodrik (1997) and Taylor (1996), creates winners and losers. Robbins (2003, 58) argues that trade liberalisation and the removal of subsidies is a 'blunt weapon' designed to benefit the economies of developed countries at the expense of the developing world. He describes how the partial transition towards a fully integrated world economy creates disparities that greatly disadvantage most developing countries. For example, many developed countries have lowered but not fully eliminated farming protection, yet they retained substantial subsidies (e.g., the United States and many European countries), while developing countries have also lowered their trade barriers, but cannot afford to provide farm subsidies. This leaves agricultural sectors vulnerable to the exploitation of foreign firms.

commerce. However, the term BMO is used generically to cover the full range of these kinds of organisations.[19]

> Through the formation of BMOs, SMEs can address the problems related to their size and improve their competitive position. It is also recognised that BMOs represent an increasingly important form of participatory development in developing countries. They can make a major contribution to the improvement of the environment SMEs operate in by serving as a vehicle for the expression of their views, taking collective action, delivering core services, and networking among members and other stakeholders (WB Group 2005, 12).

Many private firms express their views through their representative organisations. BMOs are formed to represent business views to the government and to society in general. Thus, the private sector is given a voice through these organisations. However, these representative organisations rarely represent the entire private sector. Indeed, many representative organisations are made of larger, formal enterprises. Small, informal firms are often not involved in these kinds of structures; consequently, their views are often not heard.

Many donor and development agencies (e.g., USAID, DFID, DANIDA, NORAD) provide assistance directly to BMOs, private sector firms, or non-government organisations to provide specific development services such as research, consultation, monitoring and evaluation, and the management of private sector development programmes. A recent development to the support of BMOs and of giving a 'voice' to the private sector has been the establishment of specialised advocacy funds (e.g., Busac Fund, Ghana; Business Environment Strengthening for Tanzania [BEST] Fund). These funds provide resources for BMOs to research critical business concerns and to take evidence-based proposals for reform to government.

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[19] Business membership organisations can perform a wide variety of roles, depending on their areas of interest, need and resources. For further information see: International Labour Office and International Organisation of Employers (2005).

4.8. Promoting more effective public-private dialogue

Herzberg and Wright suggest public-private dialogue (PPD) has become an important part of the private sector reform process. It can be structured or ad hoc, formal or informal, wide-ranging or focused on specific issues. "It can be initiated by forward-thinking governments, frustrated entrepreneurs, or third parties such as international donor agencies" (Herzberg and Wright 2006, 11).

International development and donor agencies are increasing recognising the role that PPD plays in promoting effective and sustained PSD. Particular attention is given in this regard to the role of PPD in business environment reform. The quality and depth of effective business environment reform is related to the intensity and institutionalisation of PPD.[20]

While many developing and transition countries have little tradition of constructive dialogue and cooperation between the government and the private sector, such dialogue changes the political economy by empowering allies of reform and enlarging the 'reform space' by increasing awareness of the scope and depth of the problem. Development and donor agencies can facilitate public-private dialogue by partially financing the dialogue process (e.g., structured and regular meetings), but should not drive the process. It is particularly important for development and donor agencies to help small and informal enterprises find a 'voice' in the processes that support PPD. PPD processes that are facilitated or supported by development and donor agencies should include a wide range of the private sector representatives and, where possible, endeavour to obtain the views of the less organised business sector.

[20] For more information on Public Private Dialogue and detailed guidance go to: http://www.publicprivatedialogue.org/

4.9. Providing a greater role for big business

Increasing attention has been given to the role of large, multinational firms in providing investments that promote economic growth and reduce poverty. The World Business Council for Sustainable Development summarises this in the following manner: "business done in new ways can help bring sustainable development to all" (World Business Council for Sustainable Development 2007, 6). Development and donor agencies, especially bilateral agencies, have promoted business-to-business or twinning programmes for some time.[21] These programmes have sought to link up businesses in developed economies with those in developing economies. In many donor countries there is demand for these programmes by the business sector. However, the new trend in providing a role of big business has two dimensions.

The first of these concerns the development of market-driven approaches to PSD focused on 'bottom of the pyramid' (BOP). This refers to the four billion of the world's poor who have needs that are currently unmet, but which could be met by the private sector (Prahalad 2005). Analysis of BOP markets can help business and governments think more creatively about new products and services that meet BOP needs and about opportunities for market-based solutions to achieve them. BOP approaches can help governments, focus their attention on reforms needed in the business environment to allow a larger role for the private sector (Hammond *et al.* 2007).

The second way in which development and donor agencies support a greater role for big business is through public-private-partnerships (PPPs). The Shell Foundation, a strong proponent of the role big business can play in supporting economic growth and poverty reduction in developing countries, suggests that big business has three main assets that can be deployed to these ends:

- A vast repository of generalised business skills that is encapsulated in people, knowledge and techniques likely to be found in great profusion, especially in big business.

[21] See for example the Austrian Development Agency (2007), Danida (Danish Government 2007).

- ‘Convening power’ – the subtle and overt ways by which a company’s track record, reputation, brand, political reach and financial clout makes other people listen and respond to what the company has to say.
- The company – sector-specific physical and market knowledge-based assets that lie at the core of the unique processes of value creation and capture on which every company relies (Shell Foundation 2005, 13).

However, to maximise the benefits of these assets, Shell argues for a better balance between risk and return. Public sector agents (development and donor agencies, governments and civil society actors) should recognise that strategies such as PPPs should be structured like business partnerships. Care should be taken to ensure the right parties are at the PPP table and clear goals should be set that make a difference to poor people, while ensuring that the partners also secure ‘returns’ they value (Shell 2005, 30). Two noteworthy examples of multiple donors engaging the private sector in this manner include the Public-Private Infrastructure Advisory Facility and the Private Infrastructure Development Group.

4.10. Collaborative funding and programme planning mechanisms

With high-level policy support provided by the Paris Declaration, collaboration among development and donor agencies is increasing. Collaboration among donors is encouraged because it shares risks and provides access to a larger pool of expertise. Key elements to successful coordination among development and donor agencies are:

- A commitment by all parties to coordination and collaboration;
- Recognition at headquarter-level of the importance of coordination in the field - to allow country offices to participate meaningfully in local coordination processes;
- Regular processes and mechanisms for information sharing;
- Leadership and facilitation - this can be provided by the host government or by a nominated development agency;
- Identifying agency competencies and capabilities, and using this as a basis for a clear division of agency responsibilities; and

- Reporting on experiences in the field - successes, challenges, emerging lessons.

Developing and transition country governments are also encouraged to work with the development community to support, enhance and, where necessary, lead coordination and collaboration efforts. In some countries, high-level government ministries convene and chair development coordination committees, in other countries this role is rotated amongst members. In the Philippines, the Philippines Development Forum (PDF) is a coordinating mechanism established by the President of the Philippines to oversee and coordinate the achievement of key development goals. The PSD activities of the PDF were led by the Department of Trade and Industry and three sub-committees were formed dealing with Infrastructure, SMEs and Business Climate.[22]

In Ghana, the Ghana Joint Assistance Strategy aims to improve the alignment of development assistance with the core business of government and the government's political and partnership cycle. It builds on commitments by development and donor agencies (referred to as 'development partners') to work toward the achievement of goals and priorities of the second Ghana Growth and Poverty Reduction Strategy and to accelerate progress against mutually defined harmonisation principles. Special focus has been given within this strategy to ongoing support for implementation of the Trade Sector Programme and the Private Sector Development Strategy. Sector-wide approaches (SWAps) for PSD and financial sector development have been established and provide the framework for coordinating external assistance in these areas (Government of Ghana 2007). In addition to budget support, some development and donor agencies in Ghana have supported the establishment of a 'pooled funding' mechanism to be placed under the Oversight Committee of the Private Sector Development Strategy.[23]

In Tanzania, the BEST programme is a cross-cutting, multi-donor financed government programme that aims at strengthening the business environment by firstly, reducing

[22] See http://pdf.ph .

[23] For a critique on the role of donors in Ghana, including the 'pooled fund' and budget support mechanisms for support of PSD see Whitefield and Jones (2007).

burden on business by removing regulatory and administrative constraints, and secondly improving quality of services provided by the Government to the private sector, including commercial dispute resolution (Tax-Bamwenda and Mlingi 2005).

4.11. Corporate governance and Corporate and Social Responsibility (CSR)

The topic of corporate governance and corporate social responsibility is a more common feature of PSD support programmes. Corporate governance has come to encapsulate the blend of law, regulation and private sector practice that enables companies to attract financial and human capital, to perform efficiently, and generate long-term economic value for their shareholders, whilst respecting the interests of stakeholders and society as a whole.

PSD support programmes attempt to address corporate governance at two levels. The first is the country level. Here, various regulatory and enforcement mechanisms are considered, such as the need for bankruptcy laws, property rights and an effective judiciary. Because a corporation cannot operate effectively if it is unable to rely on legislation and its enforcement, good corporate governance requires good political governance, and vice versa. The second level for addressing corporate governance is at the company level. Corporate governance at this level refers to the rules and regulations that shape its effective operation. Complementary interaction between these two levels is vital to ensure the effective operation of the private sector, in a manner that is both accountable and transparent.

In 1999, the OECD issued five Principles of Corporate Governance. These are non-binding principles that have been widely accepted as providing the broad framework for countries to use. It is expected that countries should then adopt their own country-owned corporate governance frameworks taking account of their unique culture and regulatory and legislative systems.

Current donor interventions in this field include DFID's Extractive Industries Transparency Initiative (EITI), which works with developing-country governments, donor agencies, regional economic groups (e.g., the New Partnership for Africa's Development (NEPAD), trans-national corporations, investors, civil society organisations, and international financial institutions to increase transparency and accountability in the extractives sector in developing countries. Similar approaches to the EITI are currently being considered for the health industry.

5. Major Debates and Controversies

This chapter examines the major debates and controversies affecting bilateral and multilateral support of PSD. While there may be variations to the degree to which some of the issues cited in this chapter may be considered debatable or controversial, each provides a particular perspective that helps to better understand the gaps in knowledge surrounding the support of PSD and how this support can lead to growth and poverty reduction.

5.1. The 'new paradigm' for PSD

One of the most recent debates around support of PSD concerns the systemic approach that is applied by a growing number of bilateral and multilateral agencies. Altenburg and von Drachenfels (2006) have recently provided a critique of what they call the 'new minimalist approach' (NMA) to PSD. This approach, exemplified by the *Doing Business* reports, the *World Development Report 2006*, and the various OECD reports cited previously in this working paper, represent a 'new consensus' that "emphasises quite a limited number of market-driven solutions and tends to disregard selective public interventions to encourage and support the private sector" (Altenburg and von Drachenfels 2006, 387). The authors argue that the NMA is characterised by the following underlying assumptions:

- Extensive government regulations hamper the formation, registration and growth of private enterprises and therefore reduce rather than increase economic growth and welfare.

- The key role of the state is to guarantee a level playing field for the private sector. Selective, for example industry-specific, public policy interventions in markets are especially distorting and often harmful to economic development.
- The exit of inefficient firms is an inevitable, and even necessary, element of structural change that should not be held back by costly efforts to preserve unsustainable entrepreneurial activities.
- Entrepreneurial spirit and capabilities are ubiquitous and unfold by themselves once a climate conducive to investment is in place; this also holds for the informal sector.
- Entrepreneurs are willing to pay for meaningful business development services, and, apart from a very few purely public goods, these may (and should) consequently be provided on commercial terms (Altenburg and von Drachenfels 2006).

It is argued that the NMA “fails to capture the complexity involved in building competitive economies and integrating the informal sector [and, in addition to the removal of external constraints to PSD], public intervention is also needed to bridge the gap between medium- and large-scale formal-sector companies and informal micro-enterprises” (Altenburg and von Drachenfels 2006, 406). Thus, the NMA argues for a greater role for the state (see below) in the form of industrial policy and skills development.

5.2. The role of the state

The NMA critique presented above argues for a “public engagement and allocation of funds” (Altenburg and Drachenfels 2006, 408) in support of PSD with the aim of promoting pro-poor development. This represents one aspect on the role of the state in support of PSD.

Verena and Menocal describe the swing in opinion among development and donor agencies regarding the role of the state, where in the 1960s, donors assumed that “states in the developing world could act as engines of development and therefore could be funded to enable investments and generate growth. However, these presumed developmental states increasingly failed to deliver, turning variously into oppressive and/or rent-seeking regimes" (Verena and Menocal 2007, 540). This led to the emergence of the Washington Consensus, which sought to reduce the size and reach of the state and reinforced the role of the market as the most effective mechanism for allocating resources and promoting economic growth.[24]

Since this time, the notion of the developmental state has re-emerged, inspired by the role of the state in the development of the south-east Asia 'Tiger Economies' and the analysis of the Asian Financial Crisis in which the role of institutions has been highlighted. The *1997 World Development Report* (WB 1997) reaffirmed the position that 'the state is central to economic and social development' and, more recently, the Commission for Africa (2005) also highlighted this thinking, identifying state capacity and effectiveness as a key bottleneck in Africa's ability to meet the MDGs.

DFID (2007) describes how the state shapes the incentives and opportunities for PSD:

> The state encompasses a range of technical functions that are vital to the creation of a favourable climate for investment and trade, which in turn will operate in the interests of society as a whole. These include the provision or regulation of public goods, such as safety and security, and infrastructure, roads, water and power, all of which are crucial to private sector development. The state should also manage the economy efficiently: controlling inflation, maintaining a stable currency, and regulating markets, finance and business effectively.[…]
>
> The state needs to identify and address the binding constraints on growth. The correct policies are often not obvious. The experience of growth in East Asia over the last few decades, for example, illustrates the key role of experimentation and learning. Sometimes the constraints are to do with the state's own role. It has been shown, for example, that businesses in poor countries face much larger regulatory burdens than those in rich countries […]
>
> The state can play a key role in enabling poor people to participate in and benefit from economic growth, but this presents special challenges. The state can draw up policies and programmes to improve incentives for, or remove biases against, employing poor people, or to overcome disadvantage or discrimination. It can address social exclusion and gender inequality, for example by ensuring equal access for women to assets such as land, livestock and financial services. And it can strengthen safety nets for those vulnerable to loss of their earnings and livelihoods (DFID 2007, 36).

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[24] See Williamson (1990).

The Donor Committee for Enterprise Development has supported the view that the principal role of government is “to provide an enabling policy, legal and regulatory environment for small enterprises and business development service providers, as well as public goods such as basic infrastructure, education and information services” (Committee of Donor Agencies for Small Enterprise Development 2001). Furthermore, says the Committee, governments can play a vital role in promoting ‘more vibrant service markets’.

Recommendation 189 of the International Labour Conference, *Concerning the General Conditions to Stimulate Job Creation in Small and Medium Enterprises*, encourages Member States to design policies promoting efficient and competitive small enterprises that provide productive and sustainable employment under adequate social conditions. To achieve this, it is necessary to create conditions that provide access to credit, foreign exchange and imported inputs and fair taxation. It is also necessary to provide effective labour laws and regulations to raise the quality of employment in small enterprises and compliance to international labour standards (ILO 1998). This approach was reinforced at the International Labour Conference in 2007 in which governments were encouraged to act as a ‘regulatory, facilitator and promoter of sustainable enterprises’, which included engaging in industrial policy initiatives, facilitating access to financial and business development services, and promoting sustainable enterprise development programmes and encouraging a “culture of sustainable entrepreneurship within specific groups, such as women, youth and disadvantaged groups, and in specific sectors and areas” (ILO 2007, 7-8).

Hitchens (2002) makes a distinction between the roles of government as a provider of services to the private sector and as a facilitator. Because experience suggests that the most effective providers of services are organisations or individuals that are close to the business community (i.e., commercially motivated and entrepreneurial, with similar backgrounds, status and structures) governments should not attempt this role. In contrast, governments may be more suited to the role of facilitator because this is a temporary intervention that uses public funds to address a specific market failure. However, Hitchens indicates there are two main requirements for effective facilitation: the capability for analysis and the flexibility to respond and engage with a range of possible market players. These conditions are not always found within government agencies. “A fundamental question for government [says Hitchens], is whether it should attempt to develop this capability to facilitate BDS markets or whether it should simply fund specialised facilitators.”

There are many who claim that government should remain a closely engaged participant in the support of PSD. Philip (2003), for example, suggests that markets cannot be relied upon to provide the development outcomes that enterprise development requires. “Empowerment does not trickle down” she writes. “Where is the agency of the poor in market development approaches, and where are the strategies to build it?”

Bannock and Darroll (2007) have argued that development and donor agencies should be wary of ‘new arguments for old approaches’, such as active industrial policy and donor-subsidised business development services. These should be very carefully assessed in light of past experience and the capacity of governments to implement them. Reinecke and White (2004) have found that the absence of clear implementation institutions and mechanisms has contributed to the limited impact of government sponsored small enterprise policies.

5.3. How to promote pro-poor growth (inclusive growth)

While all development and donor agencies subscribe to PSD as an instrument for growth and poverty reduction, not all agree on the way in which these outcomes can be achieved. Where PSD has contributed to economic growth, there have been concerns that this growth is uneven and that a special kind of growth – ‘pro-poor growth’ – is required to meet the expectations of PSD on poverty reduction.

The OECD suggests that pro-poor growth addresses income poverty and focuses attention on “policies that ensure that all sections of the poor benefit from growth, not just those nearest the poverty line or indeed those furthest away” (OECD 2004a, 13). For growth to be pro-poor it must have a high rate, it must provide opportunities to the poor to increase their incomes, and it must enable the poor to take advantage of these opportunities.

The Swedish International Development Agency (Sida) promotes the term 'pro-poor private sector development' as follows:

> Pro-poor private sector development is an instrument first and foremost to create economic growth and modernisation with direct inclusion of the poor women and men on equal terms. As such it is a tool, not an end in itself. (Nor is growth or modernisation an end in itself, but an instrument for higher societal objectives). Pro-poor PSD comprises four fundaments:
>
> 1. Competitive markets, encompassing the principle of free and fair competition, of no barriers for 'entry' of new players, and effective systems for 'exit' of failing enterprises, but also of means to address inherent market failures, and equity concerns.
> 2. Entrepreneurship, embedded in risk-taking and profit-seeking as the driving forces of change, innovation and enhanced productivity through what sometimes is called 'creative destruction'.
> 3. Private ownership manifested in clear property rights also for the poor and without discrimination in gender or ethnicity. This does not preclude public and co-operative forms of ownership as long as the principle of competition and free entry is upheld.
> 4. Decent work conditions within the private sector based on respect for human rights and fair return to labour whether in self-employment or wage labour, without discrimination in terms of gender, religion or ethnicity. Also a concern for the environment based on the principle that the world should be a better place tomorrow than today (Sida 2003).

PSD can contribute to sustained poverty reduction when there are greater opportunities for the poor to participate in markets, while also reducing their risks and vulnerability. However, there are many dimensions to poverty and its reduction: economic, human, socio cultural, political and protective, as well as the influence of gender and environmental sustainability. Thus, there is a need for PSD initiatives to focus on the full range of poverty experiences and causalities.

Some agencies have been pronounced about the importance of pro-poor growth and the role of PSD as a strategy to achieve this. USAID for example, has a strong pro-poor focus, as does Danida, NORAD and the Government of the Netherlands. This is apparent through the incorporation for pro-poor solutions into project portfolio, as well as specific programming aimed at poverty alleviation.

Other agencies, such as the International Finance Corporation and the Asian Development Bank, emphasise overall economic development instead of a pro-poor focus. Indeed, the Asian Development Bank notes that Member States have explicitly directed it to shift focus away from poverty reduction and toward economic growth.

The concern in this debate, as referred to earlier in this report, is the extent to which pro-poor issues actually reduce the rate of growth. Some argue that focusing on pro-poor issues draws attention away from the major binding constraints to growth and thereby limits growth. Others argue that growth and distribution should be treated a separate issues. In a review of Poverty Reduction Strategy Papers Stewart and Wang (2003) found a striking consistency. All the papers they reviewed were based on the premise that private sector led growth is the most effective way to reduce poverty. While some described this is 'pro-poor' (Cambodia), 'equity-based' (Burkina Faso) or 'broad-based' (Nicaragua), none considered alternative approaches to poverty reduction. Indeed, the authors found a general disregard for distributional issues of private sector led growth and, where scenarios were presented for growth, this growth was considered to have an even distribution.

Pro-poor or inclusive growth has other dimensions that affect the design and management of PSD support programmes. These include the issues of location (i.e., urban and rural PSD), gender and the informal economy. These issues are addressed later in this chapter.

5.4. The spatial dimension of PSD support

Outside of programmes designed specifically to promote rural-based and agricultural-based enterprises, very little attention appears to have been given to the support of PSD in rural and marginal areas. While there is continued interest among various development and donor agencies for local economic development and other forms of sub-national development programmes (e.g., support for decentralisation), which include support of local PSD, there is general concern regarding the extent to which national PSD support programmes benefit rural and marginal areas.

In a thorough evaluation of Sida's work in PSD in rural sub-Sahara Africa in the 1990s, Havnevik *et al.* (2003) concluded that agencies such as Sida should adopt a two-pronged approach to rural PSD. The first deals with national issues that set the national framework for rural PSD. The second deals with a more local or indigenous level to better appreciate the socio-cultural factors in order to understand where the motivation of people stems from, and which norms and value systems guide their behaviour. "Otherwise, the move into formal and better functioning institutions will be very difficult" (Havnevik *et al.* 2003, 86).

From a business environment point of view, the current trend to increase regulatory power of sub-national authorities may result in costly barriers to the operation of internal markets. Strong competition safeguards should be put in place so that there is not an explosion of superfluous regulatory requirements at the sub-national level. Sub-national PSD support programmes should not be seen as simply a local reflection of the national situation. In many countries, local governments can exert significant pressure on the national political process and sub-national PSD support initiatives can be replicated from one locality to another.

5.5. PSD support in the informal economy

The informal economy presents one of the greatest challenges facing development and donor agencies in their support of PSD.[25] The informal economy forms a large part of the

[25] The term 'informal economy' refers to all economic activities that are – in law or in practice – not covered or insufficiently covered by formal arrangements. Their activities are not included in the law, which means that they are operating outside the formal reach of the law; or they are not covered in practice, which means that – although they are operating within the formal reach of the law, the law is not applied or not enforced; or the law discourages compliance because it is inappropriate, burdensome, or imposes excessive costs (ILO 2002).

economies of many developing and transition countries, providing critical employment and income to mainly poor households. The informal economy provides a safety net for many who lose or cannot find work in the formal economy, and it includes a disproportionate number of women, young people and others from disadvantaged groups (e.g., it has been estimated that informal employment accounts for 84% of women's employment in sub-Saharan Africa).

Since the first conceptualisation of the informal sector in the early 1970s, there has been a substantial body of work dealing with the informal economy. Economists such as de Soto (1989, 2000) have examined ways in which enterprises have devised informal or extralegal mechanisms of doing business when the legal and regulatory framework was ill-suited to their needs or capacities. This has illustrated the loss of productivity and revenue for the national economy resulting from poorly designed laws and regulations.

Carr and Chen (2002) present evidence to suggest that globalisation has served to increase the numbers of informal workers and their insecurity.

> With the breakdown of a social contract between employers and employees, and the 'race to the bottom' as corporations move from country to country in search of the lowest wage rates, workers are subject to low wages, lack of benefits, and lack of security in their workplace. At the same time, governments are now less able to respond to the vulnerable and disadvantaged sections of the workforce because revenues are decreasing as tariffs and taxes are reduced as part of the globalisation process (Carr and Chen 2002, 8).

Djankov *et al.* (2000) have compared the administrative cost of registering an enterprise worldwide. A number of compelling arguments for the removal or improvement of prohibitive registration and licensing procedures has been established through the work of these authors.

However, there is little consensus on the role and utility of the informal economy in poverty alleviation and national development. Even supporters of informal micro-enterprises acknowledge that returns to such entrepreneurial activity vary tremendously and that their contribution to offsetting poverty remains unclear. For instance, Gulyani and Talukdar (2007) cite studies in which informal enterprise employment is a last resort for most women and men when compared with the option of formal employment. This, say the authors, creates confusing policy questions: Should policy makers who are concerned about poverty alleviation focus on formal jobs and education, or should they support informal enterprises? If the latter, what form should such assistance take?

The OECD suggests that the cultural context in which informality occurs is far removed from the work of international aid agencies and that these agencies should work with intermediaries to reach this social group. Special efforts must be made to work with community-based and non-government organisations, since national and local governments can sometimes block development processes in this sector (Morrisson 1995).

A number of research and policy documents in this field highlight the problems firms in the informal economy face in terms of legal and administrative barriers.[26] This approach suggests that a better business environment will lead to the formalisation of informal enterprises and a decline in the size of the informal economy. However, there is little evidence to show that this occurs.

Reinecke and White (2004) suggest that reforms to the business environment can be used to influence the behaviour of informal enterprise owner-managers in two ways. Firstly, it can be used in the most conventional sense through the rule of law. Through enforcement of laws and regulations, enterprises are prevented from behaving in undesirable ways. This usually involves the threat of fines, imprisonment or confiscation of business assets. Thus, enterprises are obliged to operate within the law and regulations of the day. The second and less conventional use of laws and regulations is to enable. Here government facilitates compliance and, hence, enterprise development through the design and implementation of laws and regulations that ascribe rights and benefits to an enterprise. The registering of intellectual property, for example, provides a right over the use of that property and protects the owner against unlawful use of that property by others.

[26] See for example: OECD (2005c).

It appears that the best way of addressing the problem of informality is through a systemic approach to the support of PSD that pays specific attention to the incentives and disincentives of formalisation as well as to the institutional and cultural framework in which poor women and men, and informal enterprises, operate. Gulyani and Talukdar (2007) suggest that greater attention should be given to a household analysis of informal firms; one that inductively analyses income portfolios of poor and not-so-poor people to better understand what kinds of jobs or enterprises they actually have and which of these are helping offset poverty.

5.6. The gender dimension of PSD support

While not necessarily a controversial or debatable issue, the gender dimension to PSD support has been given greater attention in recent times. While it is generally understood that men and women have different experiences as owners and managers of privately owned enterprises, the debate in this field is more focused on the responses to gender-based inequities. Many women's enterprise development programmes have attempted to provide assistance to women in the private sector to help them overcome the specific barriers they face. In contrast, there are increasing calls for a more systemic response to the gender-based in equities in PSD. As the new slogan suggests, 'smart economics"' includes "women into the market economy and addresses growth and equity simultaneously" (Braun 2007).

Gender analysis tools help policy makers and practitioners to better understand the realities of the women and men whose lives are affected by planned development. Principally it is about understanding culture, as expressed in the construction of gender identities and inequalities. Finnegan (2003) suggests that a gender analysis should identify the situations and circumstances facing both women and men within the target market before any PSD intervention is planned. This information would include their respective socio-economic profiles; their educational and skills base; their access to and control over economic resources; the scope and scale of economic activities; their aspirations and motivations; and their additional commitments within household, community, etc. Esim (2001) indicates how little of the current market development approaches has been successfully applied to women's enterprise promotion. She supports the proposal by Mayoux (1995) that there are two approaches to achieving women's business growth: a market approach, which aims to assist individual women entrepreneurs in increasing their incomes and expanding their businesses; and an empowerment approach which aims not only to increase the incomes, but also the bargaining power of producers.

Recent reviews of gender and economic growth in Africa show businesswomen are disproportionately disadvantaged by business registration procedures, limited access to finance and obstacles to property ownership (Ellis *et al.* 2007, Ellis *et al.* 2006). In Kenya, it has been proposed that PSD support should move "from firm-level interventions to focus more on addressing the systemic, underlying issues that create barriers for female-owned businesses" (Ellis *et al.* 2007, 95).

In 2006, the WB launched its Gender Action Plan to promote women's empowerment in the economic sectors and in particular in infrastructure (i.e., energy, transport, and water and sanitation), agriculture, PSD, and finance.[27] This will be achieved by: (1) intensifying gender mainstreaming in WB and International Finance Corporation (IFC) operations as well as through regional economic and sector work; (2) mobilising resources to implement and scale up results-based initiatives that empower women economically; (3) improving the knowledge and statistics on women's economic participation and the relationship between gender equality, growth, and poverty reduction; and (4) undertaking a targeted communications campaign to foster partnerships on the importance of women's economic contributions and execute the plan (WB Group 2006).[28]

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[27] The Gender Action Plan is supported by: Canada, Denmark, Germany, Norway, Sweden, and the United Kingdom.

[28] In an effort to promote gender responsiveness in the private sector, the Gender Action Programme will: (1) engender Investment Climate Assessments in nine countries (three per year); undertake analytical work on gender and firm productivity, and female entrepreneurship; and (3) organize workshops with policymakers, private sector representatives, and labour leaders. (WB Group 2006, 12)

At a meeting in Berlin in February 2007, the German Ministry for Economic Cooperation and Development hosted conference entitled "Women's economic empowerment as smart economics: a dialogue on policy options". In its concluding 'Call for Action', the conference agreed to "assist our partners in the south by giving greater visibility to gender equality and women's empowerment in our support towards the implementation of poverty reduction strategies e.g., by engendering Joint Assistance Strategies", as well as to "support women's voices to be fully heard in all decisions about poverty reduction, economic growth and opportunities" (German Ministry for Economic Cooperation and Development 2007, 85-87).

Increasingly gender analysis and gender-oriented programme planning are seen as being good for the economy as a whole. Because of the disproportionate number of women who are poor, and owning their own micro or informal enterprise, gender issues deserve special consideration.

5.7. PSD support and firm size

Small enterprises are a part of the broader private sector, although their ownership and management structures are very different compared to large private enterprises. Within the broad thrust of private sector development, small enterprises have a unique and significant position. While private sector development encompasses all kinds of private business endeavours, including large enterprises, multinational corporations, etc., small enterprises are by definition smaller. However, their smaller size places them at a disadvantage to larger enterprises.[29]

Compared to large enterprises, small enterprises face many disadvantages because of their smaller size. They have fewer internal resources and often need to find niche markets in which to operate. Private sector development takes a broad approach to the achievement of national development goals, but within this broad approach, the role of

[29] See, for example: Holden *et al.* (2004, p. 26), Reinecke (2002), Beck, Demirgfic-Kunt and Maksimovic (2002).

the small enterprise sector requires specific attention. "Targeting the smallest enterprises matters", says Chen (2005), "if the donor community wants to reach the poor and to reduce poverty." However, Bylund (2005) cites published evidence that a higher proportion of SMEs in the economy is associated with higher growth, but the element of those SMEs in the economy does not itself cause higher growth nor improved pro-poor growth.

There are internal and external factors that impede the competitiveness and profitability of small enterprises. Some of the main internal factors that affect enterprise competitiveness and profitability include organisational and financial management skills, business experience, financial resources, and technical or production skills. Financial and business development services are valuable interventions that can be applied to address the internal constraints of many small enterprises. However, there are also external factors that need to be addressed to help small enterprises function more effectively. These include the markets in which small enterprises operate, the policies, laws and regulations that governments put in place to regulate and promote enterprise activities, as well as the organisational arrangements that surround the enterprise. Thus, an 'enabling' external environment (i.e., an enabling business environment) is also an important element in the promotion of small enterprises.

There are competing political agendas between small and large enterprises. One view is that small enterprises deserve special attention to compensate for their disadvantages. Others claim that because this kind of attention distorts the market and is unsustainable, governments should not provide specific measures for the small enterprise sector. Getting behind the reasons for small enterprise development is important as it affects every aspect of work in this field.

In some cases, supporting small enterprises is seen as a bias against large enterprises. If the government offers incentives and support to small enterprises, shouldn't it offer these to large enterprises? Should government offer support to all enterprises regardless of their size? The WB's private sector development strategy identifies the need for interventions that support the whole private sector—through reforms of the investment climate—while recognising the need for a special focus on small enterprises:

> To complement investment climate improvements and to help unleash supply response, direct support is sometimes appropriate for formal small and medium firms as well as entrepreneurs in informal settings, for example, in rural areas. Such support may comprise both finance and advice, for example, rural credit and extension services. Several decades of attempts to provide such support have shed light on the key success factors. First and foremost, successful direct support to firms requires a sound investment climate that provides incentives to use public support well. Second, both financial and advisory support needs to be aligned with market forces. Financial terms of loans and investments should not be subsidised (WB 2002b).

From a systems perspective, attention should be given to the factors that determine enterprise growth. In many developing countries, the co-called ‘missing middle’ indicates the presence of barriers to growth. These dynamics require more, country-specific, analysis. In the meantime, many developing-country governments will want to offer special support services to small enterprises, as will development and donor agencies that want to directly support this sub-sector. The trouble remains with the number of total small enterprise population that actually manage to access and benefit from these programmes.

5.8. Entrepreneurial culture and PSD

Increasing attention has been given to the ways development and donor agencies, and their client governments, civil society actors and the business community can promote an entrepreneurial society. The promotion of entrepreneurship and the creation of an entrepreneurial culture have become critically important in the context of globalisation and the need for countries to respond to their domestic development needs, while competing in the world-economy.

The Global Entrepreneurship Monitor (GEM) is an annual report that views with business environment through the eyes of entrepreneurship. The primary focus of the GEM is on understanding the impact of entrepreneurship on national economic growth (Reynolds *et* *al.* 2002). Indeed, there are growing efforts in developed and developing countries to better understand the ways in which a more entrepreneurial culture can be created.[30]

The ILO describes entrepreneurship as “the attitude and capacity to innovate and take initiative.” Thus, entrepreneurship reflects a cultural and attitudinal platform on which other elements of the business environment are built. While the term can be applied to a range of economic and social innovations designed to solve problems, meet needs, or supply products and services, the ILO focuses on entrepreneurship as the “combination of initiative, innovation and calculated risk-taking associated with identifying market opportunities, mobilising resources, and managing them efficiently in the operation of productive, viable, and socially responsible enterprises” (ILO 2004).

The ILO’s Recommendation 189 recognises the importance of social and cultural influences on entrepreneurship and the formation of new enterprises. In light of this, it has recommended that member States endeavour to create and strengthen an enterprise culture. That is, an environment that favours initiative, enterprise creation, productivity, environmental consciousness, quality employment, good labour and industrial relations, and adequate social practices, all of which are equitable. This should include the development of entrepreneurial attitudes, through education, entrepreneurship and training. The Recommendation suggests that an appropriate means of encouraging a more positive attitude towards risk-taking should be established. One that recognises business failure as a learning experience while at the same time recognises its impact on both entrepreneurs and workers. A process of lifelong learning should be encouraged for all workers and entrepreneurs within small enterprises. It also proposes the use of awareness campaigns to promote the rule of law, workers' rights, better working conditions, higher productivity and improved quality of goods and services. This should complement the promotion of entrepreneurial role models and

[30] The European Commission (2002) Green Paper on Entrepreneurship examines a range of policy options concerning the reduction of barriers, the motivation and education of actual and new entrepreneurs and the attitudes of society at large. The paper suggests a co-ordinated approach and raises questions for debate around three pillars: (1) bringing down barriers to business development and growth; (2) balancing the risks and rewards of entrepreneurship; and (3) moving towards an entrepreneurial society. Also see European Commission (2004).

award schemes, especially those that take account of the particular needs of women, and of disadvantaged and marginalised groups (ILO 1998).

Entrepreneurship provides a useful framework for governments to assess and apply their efforts. While it is a much broader field than BDS, the promotion of an entrepreneurial culture is an endeavour for which governments are well equipped. Governments can deal effectively with a wide range of institutions (e.g., social, economic, education) to promote entrepreneurship and in doing so can set the scene for effective BDS.

6. Conclusion: Toward a Research Agenda

This chapter identifies key topics for research in support of PSD. It draws from the findings of the previous chapters and focuses on the opportunities for further research within the IDRC's GGP programme initiative. Because this paper has been commissioned to inform discussion around key research priorities, the purpose of this chapter is not to provide a detailed research brief for selected topics. Instead, the chapter briefly presents a variety of topics drawn from the discussion in the previous chapters with the aim of stimulating discussion regarding the critical information gaps that exist and the priorities for IDRC's GGP programme initiative.

Two broad areas of research are considered in this chapter. The first concerns research priorities focusing on the conceptual framework for support of PSD. This refers to research into the role PSD plays in promoting growth and reducing poverty. It concerns the causal relationships between donor support for PSD, development of the private sector, the contributions the private sector makes to economic growth, including the rate and patterns of growth, and the impact this has on poverty. In short, this concerns research that helps development and donor agencies to better understand *why* they support PSD. This research area corresponds, at least in part, to the GGP programme initiative theme on the patterns and drivers of inclusive growth.

The second area of research concerns key functional areas for support of PSD. This refers to specific aspects of development and donor agency support of PSD. That is, the *how* agencies support PSD. This research area corresponds in part to the GGP programme initiative theme on the shape, functioning, and phasing of appropriate combinations of market and non-market institutions to promote inclusive growth.

6.1. Researching the conceptual framework for support of PSD

There are a number of possible research topics that address the conceptual framework for support of PSD. This includes research into PSD supported growth that is most likely to reduce inequality and poverty. It includes research into the policy reforms that are necessary to promote enterprise development, stimulate investment, and enhance productivity. It will also involve an analysis of the determinants of labour market outcomes with a focus on equity and poverty implications by sector and geographic area.

Understanding the determinants to growth

While this topic reaches beyond the domain of PSD support, it is of critical importance to understanding better how PSD contributes to growth and how growth can reduce poverty. In a recent paper by Bannock and Darroll (2007), development and donor agencies are encouraged to re-examine the experience in Asian countries as a source of good practice and a cause for encouragement. “What Asian growth clearly demonstrates is that territories which have lain economically dormant for long periods can, in the right circumstances, start growing and in a few decades make a major impact on poverty.”[31] While there is no universal formula for growth, ‘there is pragmatic wisdom’; “if a country wants to grow, it needs to work to make itself more attractive to private business” (Bannock and Darroll 2007).

[31] In three decades, the percentage of the population of East Asia living on less than a dollar a day fell successively from 58 per cent in 1981 to 30 per cent in 1990 to 15 per cent in 2001.

Understanding the role of PSD has on inclusive growth

While many donors align their PSD support programmes with the concept of pro-poor or inclusive growth there are still many contested debates within this field. While this debate initially appears to be an ideological one (i.e., where neo-liberal approaches are contested by calls for greater state intervention), there is much more to be gained from an evidenced-based analysis of how these models have worked. This research should focus on the determinants of growth rates and patterns, and the role of the private sector.

Understanding the balance between supply and demand-side responses

There is often a tension between development and donor agencies that promote a neo-liberal approach to the support of PSD – what Altenburg and von Drachenfels (2006) called the 'new minimalist agenda' – and the interest expressed by developing-country governments in providing a more supply-side response to PSD support in the form of industrial policies and enterprise support programmes.[32] There needs to be a deeper understanding of the trade-offs and various priorities facing government that can be found in the support of PSD. This could be informed by case studies that show the way this balance has been found – or not found as the case may be.

6.2. Researching key functional areas for support of PSD

There are a number of possible research topics that can address the specific functional areas, which affect the contribution PSD can make to economic growth and poverty reduction. This includes enquiry into the poverty and equity implications of various areas of concern to the design and delivery of PSD support programmes. Thus, the focus of the research opportunities presented here focus on the ways to improve support for PSD and its desired outcomes.

[32] See, for example, the case of Ghana where the partnership between donors and government was considered a compromise on the balance between demand and supply side responses (Whitfield and Jones 2007).

PSD support and the informal economy

While a great deal of research has been undertaken on the informal economy in the last twenty years, there are specific gaps in the link between PSD and the formalisation of informal firms that need to be addressed. While emerging evidence concerning the cost of formalisation has influenced recent approaches to dealing with the informal economy, this is clearly only a part of the picture. Greater attention should be given to the systems that shape the behaviour of informal firms. Because informal employment or enterprise is a last – and in some cases the only – option for a poor woman or man, this area of enquiry must also address the broader social and economic system in which poor people live.

Enquiry into the role of institutions in supporting PSD

Economic and non-economic institutions play an important role in the business environment in which private firms operate, as well as in the processes that contribute to pro-poor growth. Institutions set the rules of the game; they create incentives and social norms. One of the main themes of this report has been the value of a systemic approach to PSD support. Institutions provide the framework for this approach and more needs to be learnt about the ways specific development outcomes can be achieved through institutional reform.

Enquiry into skills development and private sector competitiveness

Beyond support for the development of business management skills – a key ingredient in BDS – many development and donor agencies do not include skills development in their PSD support programmes. In many cases, vocational skills development and higher education is addressed outside of the PSD support portfolio. Public support for skills development is an important supply-side element of PSD support. However, developing-country governments often have inadequate resources to draw from for these purposes. Thus, there is a need for development and donor agencies to work with developing-country governments to find ways in which private investment into skills development in the private sector can be increased. This requires an approach that spans meso and micro-level interventions. Such an approach needs to improve labour market information systems and the performance of labour market institutions. It should recognise that the firm provides an ideal location for skills development that addresses the short and medium-term demands for improvements in productivity and competitiveness. Here again, development and donor agencies require information on how these systems can be encouraged; they need case studies and research that shows how these interventions can contribute to broader development goals.

Enquiry into the determinant of an entrepreneurial culture

Perhaps one of the most difficult and complex fields of enquiry concerns, not just the way in which culture affects entrepreneurial behaviour – for this is relatively well documented – but how culture can be transformed in a way that makes developing countries more competitive in the global marketplace. While this topic brings the danger of cultural imperialism and the cultural homogeneity that globalisation threatens all cultures with, it is an important field of investigation. The central area of investigation here should be on the ways in which culture can contribute to the achievement of social and economic goals. Just as there are many areas in which cultural change is recognised as a positive contributor to development (e.g., democratic change, recognition and respect for human rights) so too can culture to inform the conditions in which personal risk-taking and entrepreneurship contribute to national development goals. This is likely to be influenced by the ways young people are education as well as by the social norms and attitudes that influence behaviour.

Enquiry into the gender dimensions of PSD support

As presented in the previous chapter, there are growing concerns that the gender dimensions to PSD support are largely ignored. While some agencies have begun to address the deficits in knowledge in this field (e.g., World Bank Group, IFC), there is a need for better research. This research should not only focus on understanding the ways in which men and women have difference experiences, constrains and opportunities within the context of PSD, but also on how these issues are addressed by policy makers and programme managers. While there is a demand for more and better sex-disaggregated data, there is also a need to show how systemic responses to gender-based inequities can be addressed.

Enquiry into frameworks for PSD support impact and assessment

As presented in sub-section 3.3, assessing the performance of PSD support on the private sector and measuring its impact on economic growth and poverty reduction is a major priority for bilateral and multilateral development and donor agencies. While all agencies are required to account for the use of scarce resources for the purposes of PSD support, many bilateral agencies are searching for better answers to the questions put to them by their ministers and the taxpayers they serve. PSD support programmes require better indicators to show these links and to refine programmes in order to increase their impact on developing countries and the achievement of the MDGs. Many development and donor agencies are calling for 'compelling case studies' that show how PSD support programmes can demonstrate they have improved the performance of firms, improved the competitiveness of the private sector, and contributed to economic growth and poverty reduction.

Acronyms & Abbreviations

BDS	Business Development Services
BMO	business membership organisation
BOP	bottom of the pyramid
BRG	Better Regulation for Growth
BEST	Business Environment Strengthening for Tanzania
CIDA	Canadian International Development Agency
CGAP	Consultative Group to Assist the Poor
CSR	Corporate and Social Responsibility
DAC	Donor Assistance Committee
DANIDA	Danish International Development Agency
DFID	Department for International Development
EITI	Extractive Industries Transparency Initiative
FIAS	Foreign Investment Advisory Service
GEM	Global Entrepreneurship Monitor
GGP	Globalization, Growth and Poverty
IDRC	International Development Research Centre
IFC	International Finance Corporation
IMF	International Monetary Fund
ITC	International Trade Centre
MDGs	Millennium Development Goals
MAPP	Method for Impact Assessment of Poverty Alleviation Projects
NEPAD	New Partnership for Africa's Development
NMA	new minimalist approach
NORAD	Norwegian Agency for Development Cooperation
ODA	official development aid
OECD	Organisation for Economic Co-operation and Development
PDF	Philippines Development Forum
PSD	Private Sector Development
PSDTF	Private Sector Development Taskforce
PPD	public-private dialogue
PPPs	public-private-partnerships
SME	Small and medium-sized enterprise
Sida	Swedish International Development Agency
SWAPs	Sector Wide Approaches
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNIDO	United Nations Industrial Development Organisation
USAID	United States Agency for International Development
WB	World Bank
WTO	World Trade Organisation

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